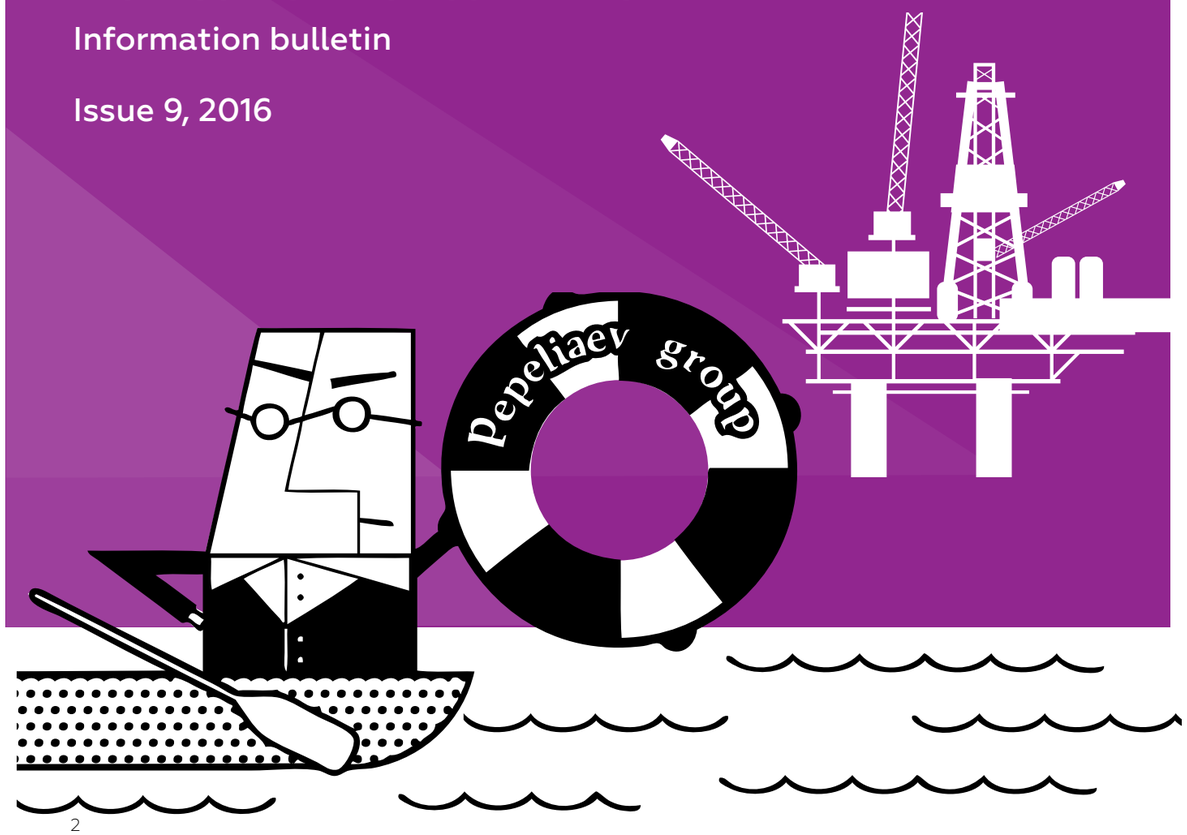
CURRENT LEGAL ISSUES OF COMPANIES INVOLVED IN RUSSIAN OIL AND GAS PROJECTS

LEGAL SUPPORT FOR COMPANIES

Information bulletin

Issue 9, 2016



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CORPORATE PROFIT TAX: CURRENT CHANGES AND THEIR INFLUENCE ON DOING BUSINESS IN RUSSIA

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1. Control over the amount of interest rates under loan (credit) agreements and the 'thin capitalisation' rules

CHANGES IN 2015

Let us remember that Federal Law No. 32-FZ "On amending the second part of the Tax Code of the Russian Federation" dated 8 March 2015 ("Law No. 32-FZ of 2015) from 1 January 2015 introduced new rules for setting market interest rates under debt obligations between related parties, including loans and credits that are recognised as controlled transactions.

Law No. 32-FZ of 2015 has set ranges for interest rates, and compliance with this means that an interest rate is set in accordance with the market level (article 269(1) of the Russian Tax Code). If an interest rate is in line with such range, then no complex transfer pricing methods need to be applied. Otherwise they should be applied.

The Russian Ministry of Finance in its letter No. 03-01-18/40737 dated 15 July 2015 states that these rules also cover related party transactions that are not recognised as controlled. However the transfer pricing rules are no longer applied to uncontrolled transactions, and are outside the scope of the first part of article 269 of the Russian Tax Code, which means that interest under such transactions is recognised in full. Therefore, the Russian Ministry of Finance again avoids interpreting the provisions literally and construes them more widely.

In addition, Law No. 32-FZ of 2015 has introduced a procedure to calculate threshold interest to apply article 269(2) of the Russian Tax Code ('thin capitalisation') based on the corresponding currency exchange rates. Law No. 32-FZ of 2015 has also established special features for calculating the threshold of interest booked as expenses from 1 July 2014 until 31 December 2016 under debt obligations that have arisen before 1 October 2014.

CHANGES IN 2016

The 'thin capitalisation' issue was further developed in Federal Law No. 25-FZ "On amending article 269 of the second part of the Tax Code of the Russian Federation with regard to the definition of the term 'controlled debt'" dated 25 February 2016 ("Law No. 25-FZ").

This law, in particular, has resolved numerous court disputes regarding the right of the tax authorities to apply the 'thin capitalisation' rules to loans between sister companies[1]. In fact, the legislature has enacted the negative case law that had developed.

The essence of the changes is that an unpaid debt will be recognised as controlled not only when the debt is to Russian organisations but also when it is to foreign organisations that are related to a foreign company.

In addition, a debt between related (but not affiliated) parties is now also recognised as controlled debt, with the threshold for related parties being increased from 20 to 25%.

Law No. 25-FZ also provides for cases when the 'thin capitalisation' rules are not applied:

- credits granted by independent banks being secured by related parties and repaid without provisional measures being applied, if neither a related party nor its related parties have in fact repaid the secured credit itself or the interest under it (from 1 January 2016);
- an outstanding debt under a debt obligation in connection with placing Eurobonds with a foreign SPV company that is a resident of a country with which Russia has a signed double taxation treaty (from 1 January 2017);
- debt obligations of Russian taxpayers to other Russian tax residents that are related to a foreign entity (a Russian resident) are not recognised as a controlled debt if a Russian resident has no debt obligations to a foreign entity that are comparable with an outstanding debt of a taxpayer to a Russian resident (from 1 January 2017).

To apply this exemption the following documented confirmation should be provided: in the first case it is confirmation of a lender bank of a Russian taxpayer debtor that the conditions established by the law are met; in the second case it is confirmation of a tax residence obtained from a competent authority of the state where the SPV company is located.

As for the third exception, for this tax exemption a confirmation will be needed that the Russian tax resident has no debt obligations to a foreign entity comparable with an outstanding debt of a taxpayer to a Russian resident.

If a Russian resident has comparable debt obligations to a foreign related entity, then only a part of the outstanding debt of a Russian taxpayer to a Russian resident can be recognised as controlled, and such part does not exceed the amount of the comparable obligation to this foreign entity.

As opposed to the transfer pricing rules, Law No. 25-FZ has reduced the list of criteria under which the comparability of debt obligations is determined:

1. the total amount (if there are several debt obligations, then they are added together to determine the comparability);
2. the time period (timeframes are considered to be comparable if the term of a debt obligation to a Russian resident does not exceed the term of a debt obligation to a foreign entity);
3. If there are differences in the currency of the debt, the obligations are recalculated in a single currency according to the rate of the Central Bank of Russia as at the date when the corresponding obligations arose.

It is noteworthy that on 18 March 2016 the Russian Supreme Court in case of New Tobacco Company has considered the situation in which two Russian organisations related to a foreign one were bound together by loan relationships. The court noted that a part of the interest was reclassified as dividends without justification and also drew the attention to the fact that a concealed dividend to the foreign company had not been identified.

Consequently, as for 'thin capitalisation' regarding tax obligations between Russian legal entities, not only have new rules been adopted, but there also is a positive case law.

[1] Companies are called "sister" companies in a situation in which the lender and the borrower are not affiliated with one another, but are affiliated with a third foreign company.

2. Controlled foreign companies

BRIEFLY ABOUT DEOFFSHORISATION LEGISLATION AND THE ESSENCE OF CONTROLLED FOREIGN COMPANIES

In 2015-2016 a star was made on improving the deoffshorisation legislation enacted at the end of 2014 (Federal Law No. 376-FZ dated 24 November 2014[2] ("Law No. 376-FZ")). This law is aimed at combating tax optimisation of Russian business and its ultimate beneficial owners with the help of foreign structures. Deoffshorisation legislation consists of three main sets of legislative instruments: the rules on controlled foreign companies ("CFCs"), the rules on determining the tax residence of foreign companies and the rules on the entity that has the actual right to the income (the beneficial owner).

The essence of the changes is that: the tax revenue to the Russian budget from the profit of foreign companies registered in offshore jurisdictions is increased, control over assets in Russia is returned, and ultimate beneficial owners must be revealed.

I would like to clarify that the essence of the CFC rules is that the CFC's undistributed profits are included in the tax base of the controlling entity at the level of Russian shareholders that are the controlling parties. Russian individuals and legal entities are recognised as controlling parties if they directly or indirectly own more than 25% of the company's capital (more than 10%, if in aggregate more than 50% is owned by Russian residents).

Law No. 376-FZ lists the grounds under which a CFC's profit is exempted from Russian profit tax. Therefore, the application of such release is restricted, including if the CFC figures in the blacklist of countries that do not ensure that information is exchanged with Russia. This list has been definitively approved by the Russian Federal Tax Service in 2016 and it came into force from 1 April 2016[3].

CHANGES IN 2015

Federal Law No. 150-FZ dated 8 June 2015[4] ("Law No. 150-FZ") has significantly changed the rules regarding CFCs. This concerns, among other things, recognising as CFCs foreign structures that do not involve a legal entity being created, including trusts. According to the amendments, when certain conditions are met, not only the founder (as was the case before the law came into force), but also the beneficial owner and other persons which can distribute the profit received by the structure (for example, the protector of a trust) are recognised as a controlling party of such structure. Therefore, the founder can be recognised a controlling party even if the founder does not have determining influence on the distribution of the profit received by a foreign structure.

Law No. 150-FZ also widens the list of grounds to exempt from taxation the profit received by a CFC – these are cases when a foreign company or non-corporate structure is recognised as a CFC, but the tax on profit which it has received yet not distributed is not required to be paid in Russia.There are three categories of companies (active foreign companies, active foreign holding companies, active foreign sub-holding companies) whose undistributed profit is not subject to tax in Russia. This has been done in order to exempt from double taxation the activity of foreign companies (controlled by Russian beneficial owners) that conduct real operational activity abroad, and holding structures created to manage such companies.

CHANGES IN 2016

Federal Law No. 32-FZ dated 15 February 2016[5] ("Law No. 32-FZ") has eliminated a number of gaps and resolved particular problematic issues. Some of these are listed below.

Double taxation has been eliminated for a party controlling dividends calculated out of profit which has already been included in the tax base of this controlling party pursuant to the CFC rules in previous tax periods.

The CFC's profit for the calculation of Russian tax is determined at the controlling party's choice: according to the audited financial statements drafted pursuant to the CFC's own law, or in accordance with the Russian rules on determining the profit tax base (chapter 25 of the Russian Tax Code). No mandatory audit of the CFC's accounting records is required: if the audit is not obligatory in accordance with the CFC's own law, then it is enough to conduct an audit pursuant to international standards.

The provisions on a preferential liquidation of a CFC[6] have been supplemented by the rule that the sale to the controlling party of securities and property rights of the CFC being liquidated is exempt from CFC's profit taxable in Russia. In addition, the term during which these provisions are in effect has been extended until 1 January 2018 (a CFC should have time to complete its liquidation by this date taking into account a number of stipulations set by Law No. 32-FZ).

An important amendment is the condition that the controlling parties are exempted from a fine and default interest for violating the legislation on CFCs if:

- the ground to recognise a party as a controlling party of the CFC is the fact that this party owns more than 10% in the CFC's capital, provided that Russian residents own a share of more than 50% in the capital; the taxpayer should provide explanations or documents confirming that the taxpayer was not aware of the fact that the participation share of all parties that are recognised as Russian tax residents in the foreign organisation exceeded 50% in the calendar year in which the notification about CFC had not been filed;
- having received from the tax authority the requirement to provide the notification about the CFC, the taxpayer should file such notification within the timeframes indicated in the requirement (at least 30 days from the date when the requirement is received).

So, if a Russian resident is recognised as a CFC then the undistributed profit of the CFC at the level of the Russian shareholders that are controlling parties will be additionally included i then profit tax base. When estimating this risk, the above legislative changes should be taken into account.

[2] "On amending the first and second parts of the Russian Tax Code (to the extent of taxing the profit of controlled foreign companies and the income of foreign organisations)"
[3] Order No. MMV-7-17/117@ of the Russian Federal Tax Service "On approving the list of states (territories) which do not share information with Russia for tax purposes" dated 4 March 2016 (registered with the Russian Ministry of Justice under No. 41486 on 22 March 2016).

According to the reports of the Russian Federal Tax Service the list will be reduced depending on improvements in exchanging information, while if there is a deterioration, specific states will be added to the list.

[4] "On amending Part I and Part II of the Tax Code of the Russian Federation and article 3 of the Federal Law "On amending Part I and Part II of the Tax Code of the Russian Federation (with regard to the taxation of profits of controlled foreign companies and income of foreign organisations)"

[5] "On amending Part I and Part II of the Tax Code of the Russian Federation and the Federal Law "On amending Part I and Part II of the Tax Code of the Russian Federation (with regard to the taxation of profits of controlled foreign companies and income of foreign organisations)"
[6] A preferential liquidation of a CFC is a liquidation in which the distribution of the CFC's property in favour of Russian tax residents is not subject to tax in Russia.

3. The rules for determining the tax residence of companies

BRIEFLY ABOUT THE ESSENCE OF THESE RULES

For profit tax purposes a foreign organisation is recognised as a Russian tax resident if its actual place of management is located in Russia, unless an international treaty provides otherwise. If a foreign company is recognised as a Russian tax resident, then all its global income will be subject to Russian profit tax at the rate of 20%.

A foreign company is not recognised as a Russian tax resident if its commercial activity is performed using its own qualified staff and assets in the state (territory) of its permanent location, with Russia having an international treaty with such state (territory) on taxation issues, and/or in a foreign state (territory) in which its standalone sub-divisions are located and with which Russia has an international treaty on taxation issues. For this purpose a foreign organisation should provide a documented confirmation that these conditions are met.

The Russian Ministry of Finance in its letter No. 03-08-17/40834 dated 16 July 2015 gave more detailed explanations regarding the application of this provision: the principal managing officers of an organisation mostly conduct their activity in the other state, the decisions connected with day-to-day business are also taken in this other state, the headquarters are located there and tax and accounting records are kept there, while assets of the company are also located there and all employment agreements are entered into there, the company conducts its production operations there and its qualified staff are also located in this other state.

CHANGES IN 2015

Law No. 150-FZ has updated the list of grounds under which, if they are present, a foreign company is recognised as Russian resident.

The company's place of management is deemed to be located in Russia if the activity of the executive body of this foreign organisation or its managing officials is performed in Russia. These criteria are referred to as the so-called initial criteria[7].

If the initial criteria are fulfilled not only with respect to Russia, but with respect to the other state, the so-called secondary additional criteria are also applied:

- the place where bookkeeping takes place or management accounting is maintained;
- the place where workflow is managed.
- the place where the company's staff is managed.
- Complying with at least one of the additional criteria is enough for a company to be recognised as a tax resident of Russia.

Law No. 150-FZ provides for cases when a foreign organisation is released from being recognised as a tax resident, and the procedure according to which a foreign company independently (voluntarily) recognises itself a Russian tax resident.

For independently recognising oneself as a Russian tax resident, there is no requirement for a double taxation treaty to be in place, which means that a company can be registered in an offshore jurisdiction, among others. In this case a foreign organisation will not be recognised as a controlled foreign company.

[7] The law excluded the criterion regarding the place for holding meetings of the company's board of directors.

CHANGES IN 2016

Law No. 32-FZ has introduced an important specification into the conditions for a foreign company to independently (voluntarily) recognise itself as a Russian tax resident; for this purpose it is enough to have a standalone subdivision, not a permanent establishment.

The Russian Ministry of Finance, in its letter No. GD-4-14/4070@ dated 14 March 2016, has explained the procedure of registering foreign organisations with the tax authorities when such organisations independently recognise themselves as Russian tax residents.

Law No. 32-FZ has corrected the conditions to apply the zero rate tax on dividends which is now available for foreign organisations which are receiving dividends from Russian companies and which have voluntarily recognised themselves as Russian tax residents.

In addition, Law No. 32-FZ specifies the conditions under which organisations that are recognised as issuers of marketable bonds on foreign capital markets are exempt from compulsory recognition as a Russian tax resident.

If a foreign company meets the above features of a Russian tax resident then its global income will be subject to Russian profit tax at a rate of 20% according to the rules of the Russian Tax Code, including transfer pricing rules and others. At the same time there is a risk of double taxation of income in Russia and in the state where the organisation is registered.

4. Rules about the person having the actual right to income (the beneficial owner)

BRIEFLY ABOUT THE ESSENCE OF THESE RULES

The main sense of the third set of deoffshorisation legislation lies in identifying the actual recipient (beneficial owner) of income if it is paid to a foreign company non-Russian resident for the purposes of applying a reduced tax rate or a tax exemption under a double taxation treaty.

Previously, in the majority of cases, it was enough to receive from a foreign company a confirmation of its residence in a state with which Russia has entered into a double taxation treaty (DTT).

The above changes has laid down that a Russian taxpayer which is a tax agent, if paying income to a foreign resident, has a right to request confirmation that the foreign company is the beneficial owner of the income.

CHANGES IN 2016

Law No. 32-FZ contains new update: to apply tax benefits under a DTT, a Russian tax agent should receive not only confirmation of the residence of the foreign company, but also confirmation that this company is the beneficial owner of the income. This means Law No. 32-FZ has transformed the previously established right into an obligation of the beneficial owner of income and of the tax agent.

Despite the fact that the amendment will come into force starting from 1 January 2017, the confirmation should be already obtained now in connection with negative trends in the case law, which emerged in 2015 and are continuing in 2016. Mainly they are based on claims of the tax authorities which in their turn arise from explanations of the Russian Ministry of Finance, most notably those formulated in the Ministry's letters No. 03-08-05/36499 dated 24 July

2014 and No. 03-08-05/64201 dated 12 December 2014:

- the tax agent's obligation to take steps to determine whether its foreign counterparties are the beneficial owners of income is not redundant for the tax agent, since such measures are required to determine the fair amount of tax.

With respect to dividends that are being paid, Law No. 32-FZ in the same way transformed the right of the tax agent and the foreign recipient of this income into an obligation: in addition to the above documents the foreign party must provide the tax agent with the following documents:

- documented confirmation that the foreign organisation recognises that there is no actual right to receive the specified income;
- information regarding the person whom the foreign organisation recognises as the actual recipient of the income (specifying the share and documented confirmation of the procedure under which such foreign organisation directly and indirectly participates in the Russian organisation which is the source of dividends), and documented confirmation of the state (territory) in which the person is a tax resident).

It is necessary to take into account the explanations of the Russian Ministry of Finance in letter No. 03-08-05/16994 in which they defined specifically the documents (information) to be requested by the tax agent from the resident of the other state to prove that this resident is the actual recipient of dividends.

When the Russian tax agent has no documents confirming residence and the actual possession of the income paid by the foreign person, and no additional documents when paying dividends, this may lead to tax as well as default interest being recovered from the tax agent[8]. The tax agent will be held liable under tax legislation.

OTHER DIFFICULT ISSUES

Many Russian taxpayers acting as tax agents interpret the definition of the actual recipient of income wrongly, which leads to either a refusal to apply DTT, or to the incorrect identification of such foreign beneficial owner, and consequently to the incorrect calculation of the amount of income.

The main mistake is that when interpreting the definition of the actual recipient of income, they usually analyse the whole holding structure and try to identify the ultimate owner of the whole business, and not the ultimate owner of the specific income received from the Russian company.

The criteria for identifying such person were formulated in letter No. 03-00-RZ/16236 of the Russian Ministry of Finance dated 9 April 2014. The Ministry highlighted that the term 'actual recipient ('beneficial owner') of income' is based on the concept of a 'beneficial owner' developed by the Organisation for Economic Co-operation and Development (the OECD). This term should be applied not in a narrow technical meaning, but taking into account such fundamental principles of the DTT as preventing abuse of the DTT's provisions and substance prevailing over form.

The Russian Ministry of Finance states the following main conditions to identify the actual recipient of income:

- not only do legal grounds need to be in place for the direct receipt of income, but such person should also be the immediate beneficiary, i.e. the person should actually obtain benefit from the income and determine its subsequent economic destiny;
- the functions being performed and the risks applied by the foreign organisation should be taken into consideration;
- benefits do not apply if they are paid within the framework of a transaction or a series of transactions performed in such a way that passive income is paid directly or indirectly through a conduit (transit or intermediate) company (a resident of a DTT state) to a person who has no right to benefits.

[8] Pursuant to the last paragraph of clause 2 resolution No. 57 of the Plenum of the Russian Supreme Commercial Court dated 30 July 2013 in this case the court imputed to the tax agent both the tax and default interest accrued until the tax agent performs its obligation to pay tax.

Law No. 32-FZ has specified the definition of an actual recipient and has directly included in this foreign structures which do not involve a legal entity being created (for example, trusts):

- a party (foreign structure without a legal entity having been created) which by virtue of direct and/or indirect participation in the organisation, control over the organisation (foreign structure without a legal entity having been created) or by virtue of other circumstances has a right to independently use and/or have at its disposal the income received by this party;
- a party (foreign structure without a legal entity having been created) on behalf of which another party (another foreign structure without a legal entity having been created) is entitled to have at its disposal the income received by the organisation (foreign structure without a legal entity having been created) specified in the above paragraph , or immediately by such other party.

Applying these changes in practice, the above explanations of the Russian Ministry of Finance need to be taken into account: the courts are guided by the same criteria when considering tax disputes.

In the light of the above and taking into account the changes, starting from 1 January 2017, it should be admitted that it is necessary to start identifying the actual recipient of income right now and to start requesting confirmation from the foreign recipients of income that they meet the requirements for an ultimate (actual) recipient of income. If upon such request the confirmation has not been provided then it is advisable for the tax agent, in order to minimise tax risks, not to apply the provisions of the DTT and to withhold tax from the foreign organisation's income.

5. Russian tax authorities receiving information from other states to ensure that the above legislative instruments are applied effectively

5.1 DOUBLE TAXATION TREATIES

In recent years, the Russian tax authorities have been requesting and receiving information regarding foreign counterparties and recipients of income from their foreign colleagues, based on DTTs and Protocols on the exchange of information that have been entered into. This information concerns individuals, as well as legal entities, the structure of ownership (possession), and specific transactions[9].

Such information has been used many times by the tax authorities against taxpayers, and the courts have usually supported the tax authorities, for example in the cases of Oriflame, Equant, Petelino, Banca Intesa and others.

The favourable outcomes for tax authorities have been reached despite the fact that currently tax officials sometimes have to wait several months for responses from other states.

But the situation will change soon, significantly simplifying and speeding up the receipt of information regarding residents of other states.

[9] According to the data of the Russian Federal Tax Service, in 2015 they were exchanging information with 58 states.

5.2 SIMPLIFYING AND SPEEDING UP THE EXCHANGE OF TAX INFORMATION BETWEEN STATES

By Federal Law No. 325-FZ dated 4 November 2014 Russia has ratified the OECD Convention on Mutual Administrative Assistance in Tax Matters[10] (the "convention") which came into force for Russia from 1 July 2015.

The convention serves as a legal ground for the exchange of all types of tax information: by request, by initiative and automatic. The convention allows information to be exchanged, including simultaneous tax audits being held with other states that have signed this document, and participation in tax audits abroad. The convention also provides for help in collecting outstanding tax in the states that have signed up to the convention, including applying provisional measures, i.e. there arises an opportunity to return a part of the funds that currently cannot be collected.

In letter No. OA-4-17/22482@ dated 22 December 2015 the Russian Federal Tax Service has explained the following specific aspects of the entry into force of the provisions of the convention for the Russian Federation:

- they cover administrative help for the tax periods starting from 1 January 2016;
- they cover tax cases related to intentional conduct which is subject to criminal prosecution in accordance with the Russian criminal law with regard to tax periods starting from 1 January 2012.

When there is mutual agreement of the parties, the provisions of the convention can be applied with regard to previous tax periods.

This convention is the legal basis for CRS (Common Reporting Standard) which is aimed at creating an international standard for the automated exchange of information regarding financial accounts and income that tax residents of one jurisdiction receive in the other. CRS obliges banks to identify the ultimate beneficial owners of CFCs, including trusts, and to send data to the tax authorities.

On 12 May 2016 Russia joined with CRS by signing the multilateral agreement of competent authorities regarding the automatic exchange of tax information[11].

This agreement provides for the automatic exchange of information regarding different types of income of taxpayers that are residents of other states (without being requested and in real time): dividends, interest, income from separate insurance products, funds from the sale of financial assets, information regarding the balance on a bank account, and payments made using the bank account[12].

Although for the automatic exchange of information with specific states Russia needs to sign treaties with such states, the Russian Federal Tax Service states that the majority of information will be received based on the above documents.

For our country this system will start working from 2018. Banks will transfer the information regarding Russian clients to the tax authorities of their state, and those tax authorities will transfer this information to the Russian Federal Tax Service.

[10] As of 29 July 2016, 98 states have signed up to the convention, including popular offshore jurisdictions.
[11] Based on order No. 834-r of the Government dated 30 April 2016.
[12] A specific list of information that the Russian Federal Tax Service receives will be enacted by a resolution of the Russian Government, and the requirements will be based on the OECD's recommendations.

5.3 INFORMATION ABOUT BENEFICIAL OWNERS OF COMPANIES

GLOBAL TRENDS

On 20 May 2015 the Fourth EU Anti-Money Laundering Directive was enacted, and it came into force on 26 June 2015. This Directive provides for the creation of a unified register of information regarding actual owners of companies and the automatic exchange of information between competent authorities of member states. To implement the Directive, the EU member states are obliged to create a special authority and to amend national legislation before 26 June 2017.

As stated above, Russia has joined the automatic exchange of tax information and starting from 2018 will technically be able to use this mechanism.

The register of beneficial owners is closed and only competent authorities (including tax authorities) will have access to it.

The Directive provides for an obligation for a legal entity registered in a state which has signed the directive to have in its possession information regarding its beneficial owners and to transfer the information in question to the competent authorities so that they can enter this information in the central register of beneficial owners. States should create a national register of the beneficial owners of corporations and other legal entities, funds and trusts created in their territories.

CHANGES IN RUSSIAN LEGISLATION

Based on Federal Law No. 115-FZ "On combating the legalisation (laundering) of the proceeds of crime and the financing of terrorism" dated 7 August 2001, banks and other credit organisations when performing operations with money and property are obliged to:

- identify the person who performs operations;
- obtain information regarding the purposes of payment and the nature of the business relationships that have developed;
- take reasonable and available measures to identify the ultimate beneficial owners.

Information regarding beneficial owners is provided at the request of the Federal Service for Financial Monitoring (Rosfinmonitoring). It can be received by the tax authorities when the Russian Federal Tax Service and Rosfinmonitoring exchange information.

On 23 June 2016 Federal Law No. 215-FZ[13] ("Law No. 215-FZ") was passed; this law amended Federal Law No. 115-FZ dated 7 August 2001 and will come into force from 21 December 2016. Law No. 215-FZ introduced the following obligations of legal entities:

- to have in its possession information regarding its beneficial owners and to take sufficient and available measures to identify them;
- at least once a year to update the information regarding its beneficial owners and record this;
- to store information regarding beneficial owners and the measures taken to identify them over a five-year period;
- to provide information confirmed by documents regarding their beneficial owners at the request of the tax authority and at the request of authorised state bodies according to the procedure approved by the Russian Government.

Law 215-FZ directly states that tax authorities are entitled to request information regarding the beneficial owners of legal entities.

Law No. 215-FZ provides that the legal entity is entitled to request from its founders, participants or other parties that control such legal entity, the information needed to identify its beneficial owners. The controlling

[13] "On amending Federal Law "On combating the legalisation (laundering) of the proceeds of crime and the financing of terrorism" and the Russian Code on Administrative Offences".
Law No. 215-FZ is based on the recommendations of the Financial Action Task Force Group on money laundering (FATF). FATF is an inter-governmental organisation that develops global standards for combating the laundering of the proceeds of crime and the financing of terrorism, and that assesses whether national legislation complies with these standards.

persons in their turn are obliged to provide all information they have to identify beneficiary owners of this legal entity.

Law No. 215-FZ also supplements the Russian Code on Administrative Offences with new provisions (article 14.25.1 of the Code). These provisions set administrative liability for a legal entity for any violation of its obligations to identify and provide the information regarding its beneficial owners.

It is likely that in practice Russian companies will face problems when identifying ultimate beneficial owners: their resources are limited, and in addition foreign parent companies presumably do not want to disclose themselves in Russia.

In the light of the above, Russian taxation rules are keeping pace with global and European rules – they all are aiming to ensure the maximum transparency of business and through this to prevent tax avoidance. In the near future, Russian legislation will undergo additional amendments to fully bring it into line with global trends.

In conditions in which legislation is changing rapidly, it is crucial to monitor these changes, assess their consequences for business and take the necessary measures in time, including restructuring specific transactions as well as the entire overall business.

CUSTOMS LAW IMPLICATIONS OF THE LOSS OF GOODS THAT HAVE BEEN RELEASED CONDITIONALLY

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General conditions stipulating that an obligation to make customs payments is terminated as a result of the destruction of goods released conditionally

Under article 200.1 of the Customs Code of the Customs Union (the "CCCU"), conditional release limits the use and disposal of goods. The extent of this limitation depends on the bases for categorising these goods as released conditionally.

For example, the intended use (article 200.2 of the CCCU) serves as such limitation for goods that acquire the status of conditionally released after being imported into the customs territory of the Customs Union, that are subject to customs duty and tax benefits, and that are tied in with limitations on their use and/or disposal. Such goods must be used only for the purposes set in the conditions for granting benefits. More specifically, chapter 26.4 of the Russian Tax Code sets a special tax regime for production sharing agreements (PSAs) entered into pursuant to Federal Law No. 225-FZ "On Production Sharing Agreements" dated 30 December 1995.

Under clause 9 of article 346.35 of the Tax Code, goods imported to perform work, which was approved in compliance with the established PSA procedure, are exempt from customs duties. Accordingly, the documented purpose of importing the goods is a mandatory condition for exempting from customs duties conditionally released goods imported to complete the work under the Sakhalin-1 and Sakhalin-2 PSAs. If an organisation does not comply with the conditions subject to which the benefits were granted, it must make customs payments after the goods are moved across the Customs Union's border.

The time period for which the goods are deemed to be conditionally released is very important, especially for goods with long life-cycles, such as fixed assets. Goods for which benefits are granted receive the status of Customs Union goods after the obligation to pay import customs duties and taxes is terminated.

The grounds on which the obligation to pay customs duties and taxes is terminated are listed in articles 211.2 and 80.2 of the CCCU. More specifically, for conditionally released goods, the obligation is terminated after five years from the release date, provided that the declarant complies with the intended use limitation throughout this period (clause 2 of article 211.2 of the CCCU).

At the same time, the conditionally released goods can be lost for different reasons (for example, through consumption or recycling/destruction). The legal effect will be attained if the goods are used for purposes that correspond to the conditions for granting the benefits.

The obligation to make customs and tax payments terminates after the destruction (irrecoverable loss) of the goods following a breakdown, a force-majeure event or natural consumption in normal transportation and/or storage conditions (clause 3 of article 80.3 of the CCCU). Furthermore, the fact that the goods have ceased to exist (the constructive loss of them) is confirmed by the fact that it is impossible to repair such goods, or that the repair costs will equal to, or be greater than, the cost of the damaged goods at the time of the breakdown[14].

Destruction of conditionally released goods and the customs and legal effects of this

It is common, following a breakdown or a force-majeure event, for the subsequent use of the goods to be impractical and so the declarant destroys the damaged goods. A similar decision is made when the conditionally released goods suffer wear and tear.

The destruction of the goods means that they are destroyed at the declarant's discretion, so the courts approach its effects differently.

In some cases, the destruction of conditionally released goods is not recognised as use other than for their purpose: the courts conclude that the destruction does not entail the obligation to make customs payments. At the same time, the courts indicate that the destruction of the goods means that they cease to exist in kind, and they are withdrawn from commercial circulation, but not that the goods are used for purposes contradicting the conditions for granting the benefits[15].

In other cases, the courts consider destruction as a legal event resulting in the obligation to pay import customs duties and taxes[16]. Thus, the impossibility of the intended use of the goods is not taken into account. When considering one such case, the commercial court indicated: *"<...> the qualitative condition of clothing destroyed by the company (either usable or unusable) has no legal effect. On the contrary, legal effect is present when conditionally released goods (regardless of their qualitative condition) are not used for their intended purposes (are used for purposes other than those stated when imported)"*[17].

Until recently these two contradictory approaches were competing in the court practice. To minimise the effects of the declarant destroying goods independently (without subjecting the goods to the customs destruction procedure), the declarant could be advised to document the goods' unsuitability for use/goods being damaged (documenting that there was a breakdown and that the goods had been written off the balance sheet), to notify the customs authorities and to document the destruction (compiling the relevant certificates and entering into destruction contracts). If the declarant followed these recommendations, there was a good chance that it would manage to prove that improper use of the conditionally released goods had not taken place.

However, in March this year the Supreme Court of the Russian Federation indicated its position on the matter of conditionally released goods[18].

In the case considered by the Supreme Court, a company challenged in the commercial court a decision of the customs authorities requiring it to pay customs duties and taxes. The decision was handed down further to the destruction of worn out equipment, which had been conditionally released with benefits granted for customs payments. The company disagreed with the decision, arguing that the loss of the goods (loss of their consumer qualities) had happened naturally through their intended use, which under customs legislation does not constitute improper use. The company did not do anything to deprive the goods of their consumer qualities. The dismantling of worn out hardware did not change the status of the goods, since hardware elements that have lost their consumer properties naturally cannot be used for their intended purposes.

The first instance court agreed with the company, deciding that the destruction of equipment does not violate the condition about the goods' intended use. The appellate and cassation courts overturned that decision, disagreeing with the company and dismissing its claim. The courts considered that the company did not follow the conditions regarding the use of goods exempted from customs payments, which gave rise to the obligation to make these payments.

The Economic Panel of the Russian Supreme Court affirmed the appellate and cassation resolutions indicating that *"the goods imported under a conditional grant of benefits must be used for their intended purpose. The goods are not imported into Russia for the purpose of being destroyed. The consequences of non-compliance with the terms and conditions regarding the use of goods which have been exempted from customs payments are provided for by customs law and involve the above exemption ceasing to have effect and the imposition on the relevant persons of an obligation to make customs payments"*.

At the same time, when analysing the Supreme Court's legal position one should bear in mind that in that particular case the goods were not destroyed completely. The declarant sold the scrap metal remaining after destruction to a third party and generated profit. It cannot be ruled out that this affected the Panel's position. But it is very probable that the courts will take the above arguments literally, thus considering destruction of released goods as them being used improperly, regardless of the specific circumstances.

Given the above legal position of the Supreme Court, declarants should refrain from independently destroying the goods which have been released conditionally, until five years elapse after the goods are released by customs for internal consumption (paragraph 2 clause 2 of article 211.2 of the CCCU). If this is impossible, it is advisable to change the customs procedure to that of abandonment to the state or destruction (paragraph 4 of clause 2 of article 211.2 of CCCU).

Consequences of conditionally released goods being stolen

The court practice is also contradictory in cases involving the legal effects of the theft of conditionally released goods. Does the obligation to make customs payments cease if the goods are stolen? The courts answer this question differently.

Some construe article 80.2 of the CCCU literally: the law does not expressly list theft as a factor that terminates the obligation to pay customs duties and taxes[19]. For example, in one case, the commercial court indicated that *"...criminal acts of third parties do not qualify as force-majeure circumstances because they are not extraordinary and objectively unavoidable in nature. Accordingly, the theft of a vehicle is not a ground for relieving an entity of its obligation to make customs payments"*[20].

The opposing court decisions are based on legal positions of the Constitutional Court (Rulings No. 168-O dated 12 May2005, No. 260-O dated 12 July 2006 and No. 1050-O dated 2 July 2013)[21]. For example, allowing for the constitutional legal meaning of customs provisions and of the Constitutional Court's comments, the Federal Commercial Court of the Far Eastern Circuit disagreed with conclusions of the customs authorities that the theft of conditionally released goods indicates that these goods have been used improperly. The court indicated as follows: "...the theft of a vehicle makes any use by the company impossible because the vehicle is actually not available to it. Furthermore, imposing an obligation to make customs payments and default interest for a missing vehicle withdrawn from the company's possession against its will takes

[14] Clause 37 of Resolution No. 18 of the Plenum of the Russian Supreme Commercial Court dated 12 May 2016

[15] See, for example: Resolution of the Federal Commercial Court of the Central Circuit dated 17 November 2010 in case No. A09-4730/2010; Resolution of the Federal Commercial Court of the East-Siberia Federal Circuit No. A33-11732/2011 dated 31 May 2012; Resolution of the Fifth Commercial Appellate Court No. 05AP-3174/2011 dated 6 June 2011.

[16] See, for example: Resolution of the Federal Commercial Court of the Volga Circuit No. A49-6097/2010 dated 15 June 2011; Resolution of the Federal Commercial Court of the Moscow Circuit No. A40-67805/11-149-396 dated 2 February 2012.

[17] Resolution of the Federal Commercial Court for the North West Circuit No. A56-19776/04 dated 22 September 2005.

[18] Ruling No. 254-PEK16 of the Russian Supreme Court dated 8 July 2016 in case No. A40-40100/2013.

[19] See, for example: Resolutions of the Federal Commercial Court of the North-West Circuit dated 3 July 2013 in case No. A56-43421/2012 and dated 23 November 2011 in case No. A56-66479/2010.

[20] Resolution 09AP-3127/2014 of the Ninth Commercial Court of Appeal dated 13 March 2014 in case No. A40-122056/13.

[21] See, for example: Resolution No. F10-1006/2016 of the Commercial Court of the Central Circuit dated 4 May 2016 in case No. A62-4885/2015; Resolution of the Presidium of the Kaliningrad Regional Court dated 25 November 2013 in case No. 44Г-24/2013.

the form of a financial liability for non-compliance with the vehicle's intended use requirement, which is imposed on the victim for a crime committed against victim's property putting the victim in an unequal position with other parties to customs relationships, which are exempt from making customs payments"[22].

Most cases of theft relate to conditionally released vehicles that were imported temporarily (article 222 of the Federal Law "On Customs Regulation in the Russian Federation"). No common approach in these types of cases has been developed in the court practice. Accordingly, in clause 37 of its Resolution No. 18 dated 12 May 2016 "On certain matters connected with the courts applying customs legislation", the Plenum of the Supreme Court explained that taking illegal possession (misappropriation, theft) of a vehicle, making impossible its mandatory exportation, could be regarded as an event that eliminates the obligation to make customs payments. The courts must check whether the declarant contacted the relevant authorities regarding the misappropriation (theft) of the vehicle and determine other circumstances of the vehicle being withdrawn from its possession, including information about the victim, the frequency of cases in which vehicles which the victim imports are misappropriated (stolen).

Thus, by itself, the fact that a vehicle has been stolen, with no regard given to other circumstances (including those of a subjective nature), is not sufficient for the obligation to pay customs duties and taxes to terminate.

Although the Plenum of the Supreme Court provided these comments with respect to the theft of vehicles under the temporary importation regime, the courts will take a similar approach when resolving disputes that arose from the theft of goods conditionally released on other grounds provided by customs law.

Should there be a theft of goods after they are released conditionally in connection with being imported into the Customs Union and exempted from customs payments, declarants are advised to take the following steps. First, they must contact the law enforcement authorities and report the theft. The theft should also be reported in writing to the customs authorities. The declarant must gather evidence confirming that it took all necessary measures to ensure the safety of the stolen property.

For example, in one case the commercial court applied clause 37 of the Resolution No. 18 of the Plenum of the Supreme Court dated 12 May 2016 and refused to invalidate the decision of the customs authorities. The court indicated that, to substantiate its claims, the declarant could *"<...> provide evidence that in this case the company was acting with the degree of caution and prudence required to properly perform its customs duties and that all measures were taken to ensure the safety of the vehicle: it was parked in a guarded parking lot, it was equipped with an alarm; and that other measures were taken; and the declarant conclusively failed to [supply such evidence] when this case was considered"*[23].

The circumstances that law lists as grounds for the termination of the obligation to pay import customs duties and taxes on goods conditionally released owing to the corresponding benefits being provided (articles 211.2 and 80.2 of CCCU) is not exhaustive. If a declarant acts properly after it loses the goods and also takes preventive measures, this will help it to avoid any unjustified imposition of the obligation to make customs payments.

[22] Resolution of the Federal Commercial Court of the Far-Eastern Circuit dated 27 December 2006 No. F03-A59/06-2/4758 in case No. A59-985/06-C24.

[23] Resolution 13AP-6442/2016 of the Thirteenth Commercial Court of Appeal dated 15 June 2016 in case No. A56-83579/2015. The Commercial Court of the North-Western Circuit applied the same approach in its Resolution No. F07-2870/2016 dated 6 June 2016 in case No. A56-45166/2012.

NEW PLENUM RESOLUTION ON CUSTOMS DISPUTES: FIRST IMPRESSIONS

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It was the Chairman of the Russian Supreme Court, Vyacheslav Lebedev, who first articulated plans to draft a new resolution of the Plenum in relation to customs disputes. He was speaking at the International Legal Forum of the Asia-Pacific Region, which took place in Vladivostok on 2 October 2015. The new resolution No. 18 of the Plenum of the Russian Supreme Court dated 12 May 2016 (the "new Resolution") contains 38 clauses. Of these, 16 are devoted to customs value issues. It replaces two Resolutions of the Plenum of the Russian Supreme Commercial Court adopted at the end of 2013 (No. 96 in full and No. 79 in part). The clarifications from Resolution No. 79 on the imposition of administrative liability are retained.

In comparison with the draft prepared by the Supreme Court's administrative office, the Resolution has been slimmed down by one clause: at the suggestion of the Russian Presidential Administration, the clarification of the following point has been removed: *"A customs authority calculating the amount of security for customs payments materially violated the principles for determining customs value and this led to such amount being calculated in an arbitrary way. In such a case, in relation to the amount of the security obtained without justification, interest would have been paid to the declarant for the excess customs payments exacted from it."*

In our opinion, this clarification would be a serious tool in the fight against political control of the customs value of goods supplied from certain countries. However, liberalism obviously also has its limits.

The new Resolution preserves the very important position that the Plenum of the Supreme Arbitrage Court has worked through according to which there is a presumption that information provided by a declarant is genuine and the burden of refuting this lies with the customs authority (clause 6). Also remaining is the provision according to which a customs authority cannot move away from a transaction price that is the basis for the customs value solely on the ground that such authority disagrees with the lower level of the price compared with pricing information available to it (clauses 5 and 7).

The new document enshrines legal positions pronounced by the Russian Constitutional Court that a transfer to supranational bodies of powers to regulate legal relationships in the area of customs should not lead to an infringement of constitutional rights and freedoms. In particular, this concerns principles of the law having effect through time (clause 2).

The clarification set out in clause 3 of the new Resolution seems somewhat strange to our eye. Only acts of the Court of the Eurasian Economic Union handed down under clause 39 of the Court's Charter may be taken into account after the examination of the relevant disputes. The thing is that those applying the law may form an incorrect impression of the decisions of the predecessor Court of the Eurasian Economic Community, which continue to have effect[24], as well

[24] By virtue of clause 3(3) of the Agreement on the termination of the Eurasian Economic Community (Minsk, 10 October 2014); see also the Decision of the Court of the EAEU dated 4 April 2016.

as of the legal status of clarifications of the Eurasian Economic Union Court that are adopted in accordance with clauses 46 and 48 of the Court's Charter.

Now, the need is enshrined to take account of the World Customs Organization's clarifications on issues concerning customs value (clause 4) and the classification of goods (clause 20). This material offers a wealth of guidance. For instance, in relation only to the issue of including royalty fees in customs value, the World Customs Organization has published around 20 clarifications with examples.

One of the main objectives of the new Resolution is to reduce the number of court disputes in relation to customs value. This is achieved by curtailing cases of adjustments on formal grounds (when an adjustment is an end in itself, the customs authorities choose whatever grounds they wish). Therefore, the new Resolution stresses that defects in the execution of documents should not lead to an adjustment of customs value (clause 7).

An expected clarification was that according to which a declarant cannot be treated as being at fault for not providing documents it does not and cannot have (paragraph 2 of clause 9). There was a danger that the new Resolution would reflect the approach laid down by the Russian Supreme Court's Judicial Panel in the context of examining specific cases in December 2015: *"it is reasonable to expect conduct"* from a declarant *"aimed at promptly gathering evidence confirming a lower price of imported goods"*. This would in effect have neutralised the position set out in the paragraph 2 of clause 9 of the new Resolution. The new Resolution states that a declarant needs to confirm only the actual acquisition of goods at the price asserted (paragraph 3 of clause 9). In this context, it is assumed that the declarant will take all reasonable measures of which it is capable to supply all information a customs authority asks for during an audit and that there are documents to prove this.

However, the breakthrough development, which will reduce formal adjustments, is the requirement for a declarant to be guaranteed a genuine opportunity to remove any doubts the customs authority may have as to whether a declared customs value is accurate (clause 8). This provision is based on Decision 6.1 of the World Trade Organization's Committee on Customs Value. Now, to ensure that a decision about adjustment is lawful, it will not be sufficient for a customs authority to rely on a customs database or on some other party's customs declaration with a greater value per kilogram for purportedly similar goods and ask for a price list, export declaration and clarification of the terms and conditions of the transaction. During the check, the customs authority must observe the requirements of the law with regard to the homogeneity of the goods. It must also take into consideration the differences in commercial conditions for supply and do this in a genuine manner as part of a dialogue with the declarant. In cases where this is not done, courts are highly likely to hold that decisions concerning adjustments are unlawful.

Doubts arise over the change in approaches to providing additional evidence in court (clause 11). No such restriction was established in the Plenum's Resolution No. 96, which fully corresponded to the position of the Russian Constitutional Court expressed in its Ruling No. 267-O dated 12 June 2006. However, the new Resolution enshrines approaches established in tax legislation (article 140 of the Russian Tax Code as amended by Federal Law No. 153-FZ dated 2 July 2103), having regard to the clarifications of the Plenum of the Russian Supreme Commercial Court in relation to applying such provision, as set out in clause 78 of its Resolution No. 57 dated 30 July 2013. This is connected with the fact that court proceedings should not be a substitute for customs control. From our point of view, which takes into account the Russian Constitutional Court's Ruling, if the court evaluates at the stage when a check is conducted whether a party's reasons for not providing evidence are valid, this infringes the party's constitutional right to challenge unjustified actions of state authorities in terms of assessing additional taxes. The court, based on the principles of fair, independent and impartial administration of justice, evaluates the evidence available in the case based on its own internal conviction. This should be founded on a thorough, objective and first-hand examination of such evidence.

At the same time, having regard to the new requirements for customs authorities, which are obliged to ensure that a declarant has a genuine opportunity to submit additional evidence, we may suppose that such valid reasons on the part of the declarant will be found. However, all the same, it is advisable to submit the customs authority on a timely basis with the documents that substantiate the declared customs value at the stage of customs declaration and at the stage when an additional check is carried out. This especially concerns transactions between related parties in customs terminology. Thus, we advise not limiting oneself to the documents and information listed in the Decision that an additional audit be held.

The clarification set out in paragraph 2 of clause 13 of the new Resolution is that: the taking of a decision to adjust the customs value in the context of customs control before goods are released is not a barrier to information about the customs value subsequently being amended at the declarant's initiative, which in practice will quickly give rise to even more questions. In particular, does this refer to making amendments to, among other things, the same information that underpinned the decision to adjust the customs value? If so, does the clarification in question allow amendments to be made to the information about the customs value if the declarant has not appealed the decision to adjust the customs value within 3 months from the date when it received such decision? If the decision to adjust the customs value was taken not before release but after the goods were released, does this clarification apply?

For example, the decision to adjust was adopted in relation to royalties being included. The three-month deadline for appealing it has expired. Is the declarant entitled to apply to the customs authority to amend the declaration because royalties should not have been included at all? Or may it ask only for a reduction in the amount of the royalties to be included, or only to have, let us say, expenses excluded on transporting the goods over the customs territory?

The Russian Finance Ministry was critical of the version of the Resolution that the Plenum of the Russian Supreme Court examined on 14 April 2016: in the Ministry's opinion, the customs value of goods imported under a leasing contract cannot be determined by the transaction value method. In clause 15 of the new Resolution, the clarifications for determining the customs value of such goods are split out into a separate paragraph. Regrettably, the outcome of such transformation was the 'loss' of the non-inclusion of the leasing company's fee for granting financing: the provision contains only a reference to the leasing company's expenses, and the fee falls outside this category. However, it is worth hoping that those applying the law will nonetheless not start to include it: this is evidenced by certain Rulings adopted by the Russian Supreme Court in March this year in relation to such disputes, as well as by the general premise that the customs value does not include expenses of the buyer that do not relate directly to the price of imported goods.

Clause 18 of the new Resolution is devoted to the conditions for licence fees (royalties) to be included in the customs value. This clause clarifies that the conditions/requirements listed in sub-clause 7 of clause 1 of Article 5 of the Agreement with regard to determining the customs value of goods must be performed collectively. In other words, for such fees to be included in the customs value, it does not suffice for only one of these conditions/requirements to be performed.

It is of paramount importance to note that, finally, the provisions of sub-clause 7 of clause 1 of Article 5 of the Agreement have been taken into account: the second condition/requirement is that the payment of royalties is a condition for the sale of the goods being assessed (directly or indirectly) for them to be exported into the customs territory of the Union. The words *"a condition of sale for export to the customs territory"* emphasizes that it is not about the rightholder's interests (i.e. without licence fees being paid, goods cannot be imported into the licensed territory), but merely about the commercial interests of a foreign seller that is not the rightholder.

Accordingly, "a sale" means a foreign seller selling goods rather than an importer selling them in the customs territory of the Union.

This clarification will allow the provision contained in the second paragraph of sub-clause 7 of clause 1 of Article 5 of the Agreement to be applied correctly. This drew a distinction between:

- licence fees being paid as a condition for the distribution or resale of the imported goods by the importer in the customs territory of the Union; and
- licence fees being paid as a condition for a foreign seller to sell imported goods for export to the customs territory of the Union.

Accordingly, the customs authority presents an insufficient argument to confirm that this condition has been met when it asserts that, without a licence agreement and without making licence fees, a declarant could not import goods into the customs territory.

The clarifications that default interest will not accrue in a case where there are advance payments or a monetary pledge, or where official clarifications have been followed (clause 21) give stronger significance to customs compliance and consulting with official bodies in terms of the application of customs legislation. Those involved in international trade are entitled to obtain such guidance from customs authorities.

The main negative change is that an application for a refund of customs payments paid (levied) in excess should be examined by a customs authority only if, simultaneously with it being filed or earlier, the declarant has initiated the amendment of the customs declaration (clause 29). In the past, the Russian Federal Customs Service proposed including a similar clarification in the Plenum's Resolution No. 96. However, the chairman of the Russian Supreme Commercial Court, Anton Ivanov, declined, since, through this, a party's right to judicial protection is restricted[25]. Regrettably, the Plenum's Resolution No. 96 does not state that the lack of an adjustment to a goods declaration is not a ground for refusing a refund or for returning an application without considering it. Despite this, in all regions of the country, uniform case law has evolved. In current customs legislation there are no provisions that would stipulate an obligation for a person filing an application for a refund of excess customs payments paid to adjust information in a goods declaration. Nor is such an adjustment named

[25] Session of the Plenum of the Russian Supreme Commercial Court on 28 March 2013, part 3 https://www.youtube.com/watch?v=qLIKDZvD7ik, 19–30 mins.

as a document that is mandatory and necessary for a refund of excess customs payments paid (see, for example, cases No. A56-74259/2014, A36-3829/2014, A09-6741/2015, A19-4060/2013, A51-11491/2015, A51-6258/2015, A51-23779/2014, A32-26884/2013, A41-52016/13, A41-34134/14, A60-46395/2014, A76-16398/2014, A56-11396/2015, and A56-33742/2015).

Accordingly, the version of clause 29 of the new Resolution proposed by the Russian Supreme Court will mean a 180 degree turnaround in this practice. The clarification at hand is capable of becoming a substantial barrier to declarants obtaining a refund of customs payments.

Under the established procedure, an application for a refund is filed with a customs office, but a request to amend a customs declaration is filed with a customs station. When an application and a request are filed at the same time with a customs office, the latter will refuse to examine both of them, citing the fact that the request should have been filed with the customs station. When requests are filed with customs stations, the response is received that a desk customs inspection has been started in relation to the declarant making a request. There is no set timeframe for the inspection, so it can take place within three years after goods are released.

It follows that the declarant has not been denied the right to make adjustments and there no omission on the part of the customs station. Court practice will show whether the declarant can use clause 31 of the clarifications regarding the right to have recourse to the court with a monetary claim when the customs authorities refuse or fail to act to allow adjustments to be made to a goods declaration (state duty, by virtue of article 333.21(1)(1) of the Russian Tax Code, is calculated as a percentage of the value (amount) of the claim) or whether the declarant must wait for a decision of the customs authority further to the results of the inspection.

After such a clarification, the number of appeals against refusals to refund payments will indeed reduce. However, regrettably, this will not be by virtue of customs authorities beginning to observe the lawful rights of declarants, but because the clarification deprives declarants of the right to judicial protection. This barrier can be overcome by way of an appeal to the Russian Constitutional Court against Article 147 of Federal Law No. 311-FZ 'On customs regulation in the Russian Federation'.

It should be noted that the new Resolution does not apply to legal relationships that emerged before it came into force. The legal position of the Russian Constitutional Court (see its Resolution No. 1-P dated 21 January 2010) is that a Resolution of the Plenum of the Russian Supreme Court containing an interpretation of a rule of law which worsens the position of taxpayers (in comparison with the interpretation previously entrenched in case law) does not have retroactive force by virtue of the principle of formal certainty. The position of the Russian Constitutional Court is significant across a range of industries, and hence is also applied on a compulsory basis with regard to the legal regulation of customs relationships (the Constitutional Court's Rulings No. 1487-O-O dated 17 November 2011, No. 1050-O dated 2 July 2013, No. 132-O dated 22 January 2014, No. 513-O dated 20 March 2014 and others).

Notwithstanding the clarification in relation to refunds (clause 29) and the new restrictions on additional evidence being presented in court (clause 11), in relation to which it is difficult to assess the consequences of their being applied in practice, as well as other shortcomings, there are more advantages in the Plenum's new Resolution. Thus, it has a positive effect on business. It is beyond dispute that the new Resolution on customs disputes will make a substantial change to case law and the practice of bodies enforcing the law.

WHAT KIND OF INVENTORY TAKING WILL HELP IN RECOVERING DAMAGES FROM EMPLOYEE?

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Virtually all employers are forced to pass tangibles to its employees. Under the labour law[26], an employee is responsible for the safety of the property, but financial liability is imposed only if damages result from his/her culpable unlawful conduct. Furthermore, the employer is forced to calculate the amount of damages and to prove that the damage was done.

In general, the procedure for holding someone financially liable is notionally divided into the following stages: 1) a violation is recorded, 2) a commission reviews it, 3) a decision is taken on imposing liability, and 4) the cost of the damage is recovered.

In our experience, the first stage - recording the violation – is the most important to ensure success in the subsequent recovery As the Plenum of the Russian Supreme Court has explained[27], the obligation to prove that actual direct damage has taken place and the amount of that damage rests specifically on the employer.

How can one prove that the company property suffered actual direct damage? First of all, it needs to be checked whether any property is recorded in the company's balance sheet. The primary approach to doing this is to compare the property in hand against the accounting data, i.e. to perform what is known as an **inventory taking[28].**

Let us discuss the timing and the manner of conducting and documenting the inventory taking, so that no complexities are experienced in the future, when attempting to hold an employee financially liable.

[26] See article 223 of the Russian Labour Code.

[27] See clause 4 of the Resolution No. 52 "On application by courts of the laws governing financial liability of employees for damage caused to the employer" dated 16 November 2006.

[28] See part 2 of article 11 of Federal Law No. 402-FZ "On accounting" dated 6 December 2011.

WHEN DO WE NEED TO PERFORM THE INVENTORY TAKING?

The number of inventory takings performed in a reporting year, the dates of them, the list of property and financial obligations that are checked during each inventory taking are all determined by the company's CEO. This does not apply to mandatory inventory takings listed in the Regulations for keeping accounts and financial reporting in the Russian Federation[29] ("Regulations No. 34n) and the Guidelines on taking an inventory of property and financial obligations[30] (the "Guidelines").

Inventory taking is required, *inter alia:*

- before preparing the annual financial statements;
- when changing accountable officers;
- when property theft, abuse or damage is discovered;
- when the CEO is changed, when over 50% of staff members leave the company and at the request of one or several staff members (in a case of collective liability).

Abuse, theft and damage could be committed by regular employees as well as by accountable officers. So, what is the difference between these two categories?

An accountable officer is an employee who has entered into a full financial liability agreement with the employer, but only in cases where the law expressly so permits. In this case, the employee must indemnify the employer in full for the actual direct damage the employer incurs. The liability of almost all other employees for the damage caused to the employer is limited to their average monthly salary[31].

Following the inventory taking, the employer identifies discrepancies between the property in question and the records, i.e. the employer calculates the amount of damage incurred. The subsequent actions of the employer depend on whether the damage was caused by an accountable officer. If the employer identifies a deficiency sustained by an accountable officer, the latter must prove that damage not was caused through his/her fault[32]. Inventory documents alone are insufficient to recover damages from regular employees: the company will have to prove that the damage was caused through the employee's fault.

The courts emphasise that if no inventory taking is performed, the quantity and the value of goods are unknown and it is impossible to determine when the deficiency occurred, thus making the damage unproven[33]. Other documents prepared by employers might not be accepted by courts as legitimate evidence; they require inventory sheets as of the times when the accountable officer was hired and dismissed[34].

INVENTORY TAKING PROCEDURE

The rules for taking an inventory are provided in the Guidelines. Court practice stipulates that violations of the inventory taking procedure invalidate the prepared documents as reliable evidence that damage has been caused[35].

Let us review the key steps of proper inventory taking.

[29] Approved by Order No. 34n of the Russian Ministry of Finance "On approving the Regulations for keeping account and reporting in the Russian Federation" dated 29 July 1998.
[30] YApproved by Order No. 49 of the Russian Ministry of Finance dated 13 June 1995.
[31] See articles 241-242 of the Russian Labour Code.
[32] Clause 4 of the Resolution No. 52 of the Plenum of the Supreme Court No. 52 "On the application by courts of the laws governing financial liability of employees for damages caused to the employer" dated 16 November 2006.
[33] See, for example, the appellate ruling of Lipetsk Regional Court dated 17 February 2014 in case No. 33-415/2014, the appellate ruling of Pskov Regional Court dated 19 August 2014 in case No. 33-1292/2014.
[34] See, for example, the appellate ruling of Rostov Regional Court dated 22 April 2013 in case No. 33-4910/2013.
[35] See, for example, the resolution of the Sovetskiy District Court of Samara dated 27 January 2016 in case No. 2-5205/2015, the appellate rulings of the Supreme Court of the Republic of Mordovia dated 20 February 2014 in case No. 33-332/2014 and of the Volgograd Regional Court dated 28 August 2013 No. 33-3996/2013.

STEP 1. CREATE THE INVENTORY COMMISSION

To perform inventory taking, the company's CEO issues an executive order creating a permanent inventory commission. When an executive order creating a permanent inventory commission is missing, the courts consider this a shortcoming in inventory taking[36].

The Guidelines contain a template for the executive order to create a permanent inventory commission and a control book along with templates of other inventory documents. Additionally, template documents to be prepared during inventory taking have been approved by the resolution of the State Statistical Service of Russia "On approving unified forms of primary accounting documents for recording cash transactions and results of inventory taking"[37] (the — "Resolution of the State Statistical Service").

Since 1 January 2013, companies have not been required to use the unified forms of primary accounting documents. Accordingly, each company may independently develop and approve its own document templates. However, still no court practice has developed of allowing as evidence documents, which were approved by companies internally. For this reason we recommend using the official document templates or templates that closely resemble them in terms of their form and content.

The employer determines the composition of the inventory commission at its own discretion: for example, the commission usually includes accountants, deputy directors, heads of department, engineers, economists and other specialists.

STEP 2. PREPARE FOR THE INVENTORY TAKING

Companies generally issue an order for inventory taking, in which they list its purpose and the timeline, as provided in the company accounting policy. The Guidelines do not require an order to be issued regarding the upcoming inventory taking and the date on which it is to be held. Still, it is advisable to issue such an order: issuing the order and making accountable employees aware of it will serve as proof that these employees were duly notified of the inventory taking and their requirement for them to participate in it.

The next step before commencing the inventory taking is for the inventory commission to obtain the latest documents concerning receipts and expenses or the latest statements of inventory transactions and cash flows. Accountable officers sign off to confirm that, by the time the inventory taking commences, all documents concerning receipts and expenses related to property have been passed to the accounting department or to the commission, and that all valuables for which they are responsible have been entered into the books while retired valuables have been written off as an expense. The courts consider the failure to obtain these signatures as a violation of the inventory taking procedure.

It is extremely important to ensure that accountable officers participate in the inventory taking. Furthermore, in addition to participating in the inventory taking, these officers also place their signatures on the inventory registers, alongside those of the commission members. After the accounts have been gone over, the accountable officers sign off to confirm that the commission has checked the property in their presence. The courts consider missing signatures and confirmations of the accountable officers as improper performance of inventory taking.

Performing the inventory taking in the absence of accountable officers (e.g. owing to them being dismissed, sick, on vacation, etc.) violates the conditions and the procedure for inventory taking: the employer does not have incontestable evidence that the accountable officer has caused the damage. The courts indicate that, with time, it becomes impossible to prove the causal relation between the employee's conduct and the damage incurred.

[36] See, for example, the appellate ruling of the Saratov Regional Court dated 9 October 2014 in case No. 33-5774.
[37] Resolution No. 88 of the State Statistical Service dated 18 August 1998.

STEP 3. PERFORM THE INVENTORY TAKING

The inventory taking involves identifying the property and comparing the actual property with the accounting data. The information about the property which is actually available is recorded in inventory registers or inventory reports prepared in duplicate at least. The model forms of these registers are provided in the Guidelines. The employer's failure to produce the inventory register when a dispute is considered constitutes grounds for ruling the inventory taking illegal.

The Guidelines determine rules for completing the inventory registers. Failure to follow these rules causes the inventory taking to be invalid. For example, the court declared an inventory taking invalid because registers contained multiple erasures, unverified corrections and crossings out.

After checking the property which is actually available, the data obtained is checked against the accounting data. The results are recorded in inventory check sheets (certificates).

STEP 4. FINALISE THE INVENTORY TAKING RESULTS

The inventory taking is followed by preparing the documents listed in the table.

DOCUMENT	WHAT DOES IT REGULATE	DOCUMENTS IF ACCOUNTABLE OFFICER IS ABSENT/REFUSING TO COOPERATE
The Order to create the inventory commission	The composition of the inventory commission	If the accountable officer refuses to participate or avoids participating in the inventory taking, representatives of external agencies need to be included in the commission
The Order to perform the inventory taking signed to acknowledge that the employee has seen it (recommended)	Confirms that the employee was properly notified about the need to participate in the inventory taking	The certification of accountable officer's refusal to read the order, the certification of employee's absence from work, letter/telegram to the accountable employee regarding the time of the inventory taking
The inventory register signed by the accountable officer and the commission members	Confirms that the accountable officer took part in the inventory taking, confirms that the accountable officer has no complaints about the inventory taking procedure	The register signed by all commission members and (recommended) by representatives of external agencies included in the inventory commission; the certification of the accountable officer's refusal to sign the register or the certification of his/her absence
The inventory check sheet signed by the accountant and the accountable officer indicating his/her approval of the inventory taking results	Sets the quantity of any shortfall and its value, certifies the accountable officer's approval of the results of the property recount	The inventory check sheet signed by the accountant, who checked that it was correctly completed, the certification of the accountable officer's refusal to sign the inventory check sheet or certification of his/her absence

Even if the accountable officer agrees with the inventory results, this employee can still subsequently go to court to challenge the recovery of amount of any shortfall, and the court will carefully study whether the procedures were performed lawfully. Accordingly, the employee's approval of the results of the inventory taking and of any shortfalls identified does not mean that the inspection is over. The employer must request a written explanation from the accountable officers and must continue its inspection, concluding this with the commission's decision regarding its outcome.

Thus, timely and high-quality inventory taking is a prerequisite for successfully recovering damages from employees. This is confirmed by the extensive court practice.

Please keep in mind that damage not exceeding the employee's average monthly salary is recovered from a culpable employee by order of the employer. The law allows a one-month period from the date when the final amount of the damage is determined for the employer to issue this order. After this period, damages can only be recovered through litigation.

AUTHORS OF THE BULLETIN

PAVEL KONDUKOV

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WHAT HE SPECIALISES IN

For more than 14 years Pavel has been specialising in tax law, including in tax advisory work and tax litigation.

For the last 7 years Pavel has been also advising on the legislation which regulates the activities of oil and gas companies at deposits of hydrocarbons, including in relation to subsoil resources, the continental shelf, and production sharing agreements (PSAs).

Pavel is actively involved in preparing draft laws and amendments in the above fields of expertise.

HIS MAIN ACHIEVEMENTS

- defending clients in more than 100 tax disputes, including changing negative case law in previous years, and advising on numerous issues associated with numerous issues associated with the application of tax law;
- drafting memoranda regarding the application Russian tax law in disputes submitted for resolution in international arbitration forums;
- advising major oil and gas companies with regard to their activities at oil and gas deposits, including among other things, developing draft laws;
- drafting a new PSA and negotiating with state authorities;
- participating as an expert in various meetings and expert boards of the State Duma Energy Committee and the Committee on Economic Policy, Innovative Development and Entrepreneurship;
- opening an office in Yuzhno-Sakhalinsk and developing the Far East Practice.

HIS MAJOR CLIENTS

Russian Ministry of Energy, Rosneft, Total, Yamal LNG, Shtokman Development AG, Caspian Oil and Gas Company, Elvari Neftegaz, Parker Drilling, Haliburton, KCA DEUTAG Drilling, Transneft, Sovkomflot, Fortum, Sakhalin-Shelf-Service, Kentech Sakhalin Technical Services, ENKA, METRO Cash&Carry, BMW, Volkswagen.

WHAT THEY SAY

In 2013-2015, the international directories The Legal 500 and IFLR1000 mentioned Pavel as one of the leading Russian lawyers in the oil and gas industry.

In 2016 The Legal 500 again included Pavel in its “Energy and Nature Resources” section and commented: “Pepeliaev Group’s offshore projects team is headed by the ‘outstanding’ Pavel Kondukov, who advises on tax legislation and regulatory issues affecting large-scale projects”.

Pavel’s project resulted in Pepeliaev Group winning the ITR European Tax Award in the European Tax Transaction of the Year in the Energy Sector category in 2014.

ANDREY MIKULIN

Head of Sakhalin Office

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WHAT HE SPECIALISES IN

Andrey specialises in administrative, financial, customs and civil law. He has fifteen years of experience of advising major Russian and foreign companies on various legal issues, including legal support of large-scale projects in the fishing, construction, raw materials and processing industries. Andrey has extensive experience of representing clients before state executive authorities and the state commercial courts.

HIS MAIN ACHIEVEMENTS

- defended major foreign entities in state commercial courts regarding the recovery of customs duties that had been overpaid under the Sakhalin-1 Production Sharing Agreement;
- provided legal support under a project that involved an oil pipeline being constructed, including legal advice and representing clients in the context of civil, land and environmental legislation;
- has many years of experience in drafting legal expert reviews for the management of seaports when trans-actions are concluded with respect to sea vessels;
- represented a major foreign corporation in a state commercial court in relation to whether corporate profit tax had been lawfully assessed;
- Andrey has more than 10 years of experience in legal support for large corporations, i.e. customs agents, regarding the customs clearance of goods, including those imported and exported under oil and gas projects and also in defending corporations in administrative offence cases.

HIS MAJOR CLIENTS

Kentech Sakhalin Technical Services, Parker Drilling.

WHAT THEY SAY

Chambers Europe: “Clients say that ‘the team works very quickly and is ready to help at any time under any circumstances”.

ALEXANDER KOSOV

Partner

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WHAT HE SPECIALISES IN

Alexander specialises in customs law, currency law and foreign trade regulation, including the WTO rules. For over 18 years he has been providing legal assistance to clients with respect to structuring transactions and business models taking into account foreign trade regulation, possible changes of rates of customs duties, customs value, classification of goods for customs purposes, applying customs benefits and preferences, using simplified customs procedures, currency control, technical regulation, protective measures, subsidies. He also handles challenges to the decisions of the customs authorities in pre-trial and in court proceedings, as well as challenging regulations, including before the Court of the Eurasian Economic Union.

HIS MAIN ACHIEVEMENTS

Alexander's professional background has involved defending clients in more than 300 cases in which he has acted for major Russian and foreign companies.

His achievements include:

- developing a regulation regarding the regime of 'industrial assembly' for major car manufacturers and assisting 6 companies in entering into contracts;
- identifying a code according to the Commodity Classification for Foreign Trade with a zero rate of import duty for the manufacturing of cars;
- owing to the documents he had prepared confirming that the relationship did not influence the price of goods, we managed, at the pre-trial stage, to remove the claims of the customs authorities regarding a significant reduction in purchase prices resulting from transfer of supply from independent distributors to the client's Russian subsidiary;
- successfully representing a major Russian manufacturer when challenging in a commercial ('arbitration') court a decision of the customs disallowing the application of customs benefit in the amount around USD 20,000,000.

HIS MAJOR CLIENTS

FIFA, Samsung, Renault, Johnson & Johnson, P&G, Sanofi, Nike, IKEA, Sovcomflot Varandey.

JULIA BOROZDNA

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WHAT SHE SPECIALISES IN

For over 14 years Julia has been providing legal support to clients (primarily, multinational and major Russian companies) on the full range of legal issues that may have an impact on their business from the perspective of employment and migration law. Julia offers solutions for protecting clients' business interests and mitigating their risks.

She has extensive experience in pre-trial settlement of labour disputes as well as in litigation.

HER MAIN ACHIEVEMENTS

- for several years in a row Julia has been recognised as one of the leading experts in employment law in Russia by authoritative international legal guidebooks, including The Best Lawyers, PLC Which Lawyer, Chambers Europe, European Legal Experts Guide, Who's Who Legal: CIS, and The European Legal 500 Guide;
- under Julia's leadership, the Labour and Migration Practice of Pepeliaev Group has become one of the largest and most successful in Russia;
- in 2012, Julia was appointed Deputy Chair of the Labour Law Subcommittee of the Association of European Business and in 2014 she was elected to chair the Subcommittee;
- Julia is the author and co-author of numerous articles on employment, migration, personal data, trade secret protection, and other legal issues. These have been published in such newspapers and journals as The Moscow Times, Vedomosti, Corporate UK, New Legislation and Legal Practice, General Director, Corporate Lawyer, Trudovyie Spory, Kadrovoye Delo, Kadrovik.ru, Nalogoved, Getting the Deal Through, and many others;
- Julia is a member of the experts' board of the Trudovyie Spory magazine.

HER MAJOR CLIENTS

ALROSA, British American Tobacco, Allianz, Parker Drilling, Nokia, Nike, and P&G.

WHAT THEY SAY

Julia Borozdna has been noted for being "client-oriented" and "very professional in solving complicated tasks, as well as in urgent cases" by The Legal 500: EMEA. Chambers Europe viewed Julia as a "serious player with terrific skills." Clients regard Julia Borozdna as a leader, who provides "clear and reliable support" (Chambers Europe).

ROMAN GEREBTSOV

Senior Associate

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WHAT HE SPECIALISES IN

Roman has over 10 years of experience specialising in labour and migration law along with personal taxation. His experience includes advising the largest international and Russian companies on various labour and tax law issues and structuring job placements in Russia and from Russia, taking account of the migration, labour and tax implications.

Roman also has vast experience in developing the foreign policies of international companies and adapting them to local standards. These include remuneration and incentive schemes for company employees.

HIS MAIN ACHIEVEMENTS

Roman has a track record of advising and representing a host of clients that are major Russian and foreign companies.

His achievements include:

- successfully representing a subsidiary of one of the foremost foreign retailers in relation to claims filed by the state labour inspectorate with regard to over 300 employees;
- representing a large oil company in a wrongful dismissal lawsuit, filed by an employee;
- assisting a large international telecommunications company with restructuring its relations with employees.

HIS MAJOR CLIENTS

IKEA, Nokia, Sanofi, Nike, Reuters, Oriflame, Volkswagen, British American Tabaco.

WHAT THEY SAY

The Employment and Migration Law Practice of Pepeliaev Group has a deep knowledge of labour legislation and provides highly valuable and professional advice (Legal 500, 2016).

YULIA ZHIZHERINA

Associate

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WHAT SHE SPECIALISES IN

Yulia specialises in labour law: HR record management, HR audits, developing internal regulatory acts and corporate standards, the dismissal of employees on various grounds, pre-trial settlement of labour disputes, occupational safety, investigation of accidents, and labour law training.

HER MAIN ACHIEVEMENTS

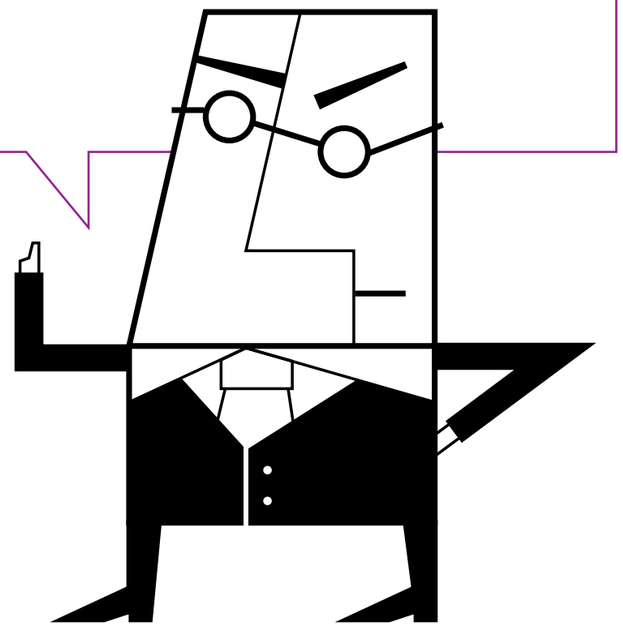
- successful implementation of the project for keeping track of total working hours at a large foreign company. The project allowed the hours of overtime to be reduced, thus, substantially reducing the payroll costs;
- drafting termination documents and negotiating with employees in several large foreign companies. The documents and negotiations allowed employees to be dismissed without adverse consequences for the companies;
- reinstating military service registration in a major foreign firm, which largely reduced the risk of the company being held liable for corresponding violations;
- holding seminars, training sessions and webinars on labour law, which have been very successful among clients;
- preparing legal opinions on employee business trips, introduction of remote work, irregular working hours, benefits for residents of the northern regions, recording the time worked, investigation of accidents, and on dismissing employees on various grounds;
- writing articles for law magazines.

HER MAJOR CLIENTS

Nike, BD, Apple, Nokia, IKEA, BP.

WHAT THEY SAY

What the team is known for Leading domestic firm, acting on regulatory and day-to-day matters alongside labour disputes (Chambers Europe).



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