

ClientAlert

Tax

March 2015

New Interest Rate Thresholds

On 9 March 2015 Federal Law No. 32-FZ “On Amending Part II of the Tax Code of the Russian Federation”, dated 8 March 2015, entered into force.

The Law is aimed at softening the negative tax effect on borrowings resulting from the recent ruble devaluation and changes the interest rate thresholds for determination of a debtor’s deductible expenses and a creditor’s taxable income as well as the rules on calculation of the “controlled debt : equity” ratio for the purposes of *thin capitalization* restrictions.

Interest amount thresholds for controlled debt

For the purpose of calculating *controlled debt* which, under *thin capitalization* rules, may not exceed 3 times equity, the following interim rules are introduced with effect from 1 July 2014 until the end of 2015:

- the ruble equivalent of *foreign-currency nominated controlled debt*¹ at the end of a reporting/tax period is to be calculated based on the Bank of Russia exchange rate valid at the relevant date, subject to a cap which is set at the exchange rate applicable on 1 July 2014 (RUB/USD 33.8434; RUB/EUR 46.1827);²
- the calculation of *equity* will now exclude any positive/negative “foreign currency exchange differences” that arise with regard to foreign-currency nominated receivables/payables after 1 July 2014.

These interim rules are applicable to *controlled debt* which arose before 1 October 2014.

Interest rate thresholds

The Law leaves unchanged the rule that from 2015 in *uncontrolled transactions* (borrowings) the *actual interest rate* determines the amount of the debtor’s deductible expense and taxable the creditor’s income; and introduces the following:

- with regard to *controlled transactions* (borrowings),³ the interest rate thresholds (currently applicable to borrowings from banks only) are extended to non-banking borrowings;
- with regard to *ruble borrowings*, the interest rate thresholds are softened.

¹ *Controlled debt* is determined in accordance with Article 269(2) of the Tax Code and includes debt obligation to (or secured by) (a) foreign company that directly/indirectly owns more than 20% in debtor’s capital or (b) its Russian affiliates.

² Compare: the Bank of Russia currency exchange rate on 31 December 2014 equaled to RUB/USD 56.2584 and RUB/EUR 68.3427.

³ *Controlled transactions* are determined in accordance with transfer pricing rules in Article 105.14 of the Tax Code.



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| Types of borrowings | Interest rate thresholds | To whom applicable |
|---|--|--------------------|
| From 01.12.2014 until 31.12.2014 | | |
| Any borrowings in ₪ | CBR ref. rate ⁴ × 3.5 = 8.25% × 3.5 = 28.875% | Debtor's expenses |
| From 01.01.2015 | | |
| <i>Uncontrolled transactions</i> | Actual interest rate | Debtor's expenses |
| <i>Controlled transactions</i> (from banks and others) | <ul style="list-style-type: none"> ■ Actual interest rate – if <i>above</i> the min and <i>below</i> the max interest rate thresholds (see the next chart) ■ Actual interest rate adjusted by general transfer pricing rules (if outside the max/min thresholds) | Creditor's income |

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| Currency of borrowing | Interest rate thresholds | | |
|-----------------------|---|--------------------------------|--------------------------|
| | Min for income | | Max for expenses |
| ₪ | <i>domestic borrowings</i> ⁵ | <i>cross-border borrowings</i> | <i>any borrowings</i> |
| 2015 | CBR key rate ⁶ × 0 | CBR ref. rate × 0.75 | CBR key rate × 1.8 |
| 01.01 – 01.02 | 17% × 0 = 0% | 8.25% × 0.75 = 6.1875% | 17% × 1.8 = 30.6% |
| 02.02 – 15.03 | 15% × 0 = 0% | | 15% × 1.8 = 27% |
| 16.03 – ... | 14% × 0 = 0% | | 14% × 1.8 = 25.2% |
| from 2016 | CBR key rate × 0.75 | | CBR key rate × 1.25 |
| € | EURIBOR ⁷ + 4% | | EURIBOR + 7% |
| ¥ (CNY) | SHIBOR ⁷ + 4% | | SHIBOR + 7% |
| ¥ (JPY), CHF | LIBOR ⁷ + 2% | | LIBOR + 5% |
| <i>Others</i> | LIBOR ⁷ + 4% | | LIBOR + 7% |

4 CBR ref. rate means the refinance (lending) rate of the Bank of Russia. From 14 September 2012 this rate was 8.25%.

5 Domestic borrowings mean borrowings where all of the parties to the transaction (related persons) have either their place of incorporation, place of residence or place of tax residence in the Russian Federation (according to Article 105.14 (2) of the Tax Code).

6 CBR key rate means the key rate of the Bank of Russia, introduced on 13 September 2013 at the rate of 5.5%, increased to 17% from 16 December 2014, decreased to 15% from 2 February 2015 and further decreased to 14% from 16 March 2015.

7 EURIBOR, SHIBOR and LIBOR mean European, Shanghai and London interbank offered rate accordingly.