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FORTE TAX & LAW

Transfer Pricing: Changes in 2024

DEAR CLIENTS, BUSINESS PARTNERS, AND FRIENDS,

Some significant changes in the regulation of transfer pricing [1] came into effect on January 1, 2024. In our opinion, there are two key objectives that they pursue:

1) One is to encourage taxpayers to take a more conservative approach to setting transfer prices by raising costs for businesses where transfer prices are found to be inconsistent with the arm's length principle; and

2) The other is to ease the administration of transfer prices to for tax authorities, sometimes by increasing the administrative burden on businesses.

We will take a closer look at these changes below.

Truly yours,

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1. Federal Law No. 539-FZ of November 27, 2023 On Amendments to Parts I and II of the Russian Tax Code, Certain Legislative Acts of the Russian Federation, and the Invalidation of Certain Provisions of Legislative Acts of the Russian Federation

1. INTERDEPENDENT PERSONS

The Russian legislature has expanded the formal grounds for recognizing persons as interdependent [2]. Thus, the existing grounds for recognizing persons as interdependent have been expanded to include the following:

- a) Entities, if they are more than 25% owned by relatives, directly or indirectly, or relatives have the power to appoint or elect the chief executive officer or 50% or more of the members of the collective executive body or the board of directors.

For example, Citizen A holds a 30% share in Company A, and his brother holds a 30% share in Company B. In this case, Companies A and B will be recognized as interdependent;

- b) A controlled foreign company (CFC) and its controlling person; and
- c) Controlled foreign companies (CFCs) that have the same controlling person.

It should be remembered that the ground for recognizing a person as controlling a CFC is not only direct or indirect ownership of a certain share in an entity, but also the ability to control such an entity in the interests of their own or those of their spouse and minor children [3].

These changes are not significant as such persons could be recognized as interdependent before. However, to do so, tax authorities were required to prove in court that the relationship between these persons is such that they can influence the terms or the results of their transactions, or the economic outcomes of the activities of these persons or the activities of the persons that they represent [4].

2. Article 105.1(2) of the Russian Tax Code has been supplemented with subsections 12 to 14.
3. Article 25.13(6) of the Russian Tax Code
4. Articles 105.1(1) and 105.1(7) of the Russian Tax Code

2. CONTROLLED TRANSACTIONS

The list of controlled transactions has been expanded to include transactions with unincorporated foreign entities, if the place of residence, the place of registration, or the place of tax residence of the respective foreign entity or one of its participants (shareholders, trustees, or other persons) or of beneficiaries, is a state or territory included on the list of offshore zones approved by the Russian Ministry of Finance [5]. Transactions with a foreign entity will be subject to control, if the total amount of such transactions exceeds RUB 120 million a year.

As you may remember, the inclusion of so-called "unfriendly countries" on the list of offshore zones last year significantly increased the number of transactions recognized as controlled. Please read our [legal alert](#) on this matter. For the purposes of recognizing transactions as controlled, the new list of offshore zones will be used starting from January 1, 2024 [6].

To mitigate the negative consequences of this step for Russian taxpayers, changes have been made to Article 105.14(4) of the Russian Tax Code, providing that the following transactions will not be recognized as controlled:

5. Article 105.14(1)(3) of the Russian Tax Code
6. Letter No. 03-12-11/1/126454 of the Russian Ministry of Finance dated December 27, 2003

- 1) Transactions with an export credit agency or a bank that simultaneously meet the following requirements:
 - a) The place of registration or the place of tax residence of such an agency or a bank is a foreign state, the agreement for the avoidance of double taxation with which has been suspended by the Decree of the Russian President;
 - b) The parties to the transaction are not recognized as interdependent;
 - c) The transaction is not a controlled transaction in the area of foreign trade in goods provided for in Article 105.14(5) of the Russian Tax Code.
 - d) The transaction is not a controlled transaction involving the resale of goods (performance of work, provision of services) that is made with the participation (through mediation) of persons who are not interdependent, and where intermediaries do not assume any risks, do not use any assets, and do not perform any functions other than arranging for the resale of goods (works, services) from one person to another interdependent person.

2. CONTROLLED TRANSACTIONS

- 2) Transactions that result in the taxpayer incurring debt obligations related to the placement by foreign entities of traded bonds (in Article 310(2)(8) of the Russian Tax Code);
- 3) Transactions with foreign entities that simultaneously meet the following requirements:
 - a) The place of registration or the place of tax residence of such an entity is a foreign state, the agreement for the avoidance of double taxation with which has been suspended by the Decree of the Russian President;
 - b) Contracts (agreements), under which these transactions were conducted, were entered into before March 1, 2022;
 - c) The price determination procedure or pricing methods (formulas) used in these transactions have not changed after March 1, 2022;
 - d) These transactions are not in compliance with the conditions that were in force as of March 1, 2022 for recognizing transactions as controlled transactions according to Articles 105.14(1) and 105.14(3) of the Russian Tax Code.

3. SECONDARY ADJUSTMENTS

The concept of "secondary adjustments" has been incorporated into the Russian Tax Code [7]. This concept is not a Russian invention and is mentioned both in the OECD Commentaries on the Model Tax Convention and in the legislation of several countries. Moreover, it was used in Russia before, but its use was episodic and unsystematic.

In simple terms, a secondary adjustment is the reclassification, for tax purposes, of the positive difference between the actual and market price in a controlled transaction.

Let us explain it by giving an example. Company A from Country A received 100 monetary units from the interdependent Company B from Country B for the goods supplied. The market price of the goods was recognized as 85 monetary units. In this example, Company A received 15 monetary units more for its goods than in the situation when the transaction with Company B would have been made on market terms (based on the arm's length principle). Thus, the actual distribution of profit in the transaction does not correspond to the result that would have been obtained if the

controlled transactions had been conducted on market terms. Secondary adjustments allow the reclassification of the excess income received by Company B into some other income and the levying of tax on it.

According to the OECD Commentaries on the Model Tax Convention, such excess income can be reclassified as (1) dividends, (2) investments in capital, or (3) a loan [8]. The Russian legislature chose to reclassify it as dividends. Thus, according to the new Article 105.3(6.1) of the Russian Tax Code, if the price actually applied in a transaction between interdependent persons, one of which is a tax non-resident of Russia, differs from the market price, and such difference became the basis for a tax base adjustment, the income arising for such a non-resident in the amount of the corresponding adjustment will be equated with the dividends received from sources in Russia and will be taxed in Russia.

7. Articles 105.3(6.1) and 105.3(6.2) of the Russian Tax Code

8. Para. 4.68 of the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations (as amended on January 20, 2022).

3. SECONDARY ADJUSTMENTS

Transactions Subject to Secondary Adjustments

Secondary adjustments will be made only to transactions between interdependent persons, a party to which is a person who is not a tax resident of Russia. This means that secondary adjustments will not, inter alia, be made to:

- a) To controlled transactions between residents of Russia;
- b) To controlled transactions between independent counterparties. For example, transactions with independent counterparties from offshore zones, or in the area of foreign trade in goods that are included on the list of product groups provided by Article 105.14(5) of the Russian Tax Code.

Date of Income Recognition as Dividends

The date of income recognition by a party to a controlled transaction is deemed to be the last day of the calendar year, in which the transaction between interdependent persons, to which a secondary adjustment is made, was conducted.

Exception from the Rule on Secondary Adjustments

The law provides that secondary adjustments will not be made if a non-resident returns excess income to a resident. However, for this purpose, the return must meet several conditions:

- 1) The income arises as a result of an adjustment to the tax base made by the taxpayer. If the primary adjustment to transfer prices is made by tax authorities, the return of excess income will not exempt from a secondary adjustment.
- 2) The excess income is returned to the resident's bank account with a bank located in Russia. Returns to foreign bank accounts will not avoid a secondary adjustment. At the same time, in practice, European banks may be reluctant to transfer funds to banks accounts in Russia, which may create difficulties in meeting this condition.

3. SECONDARY ADJUSTMENTS

- 3) A return is made in cash. This means that offsetting and other forms of termination of obligations will not avoid secondary adjustments.
- 4) A return is made no later than the deadline set for payment of tax for the tax period, in which the transaction was conducted between interdependent persons. If the return is made after this date, then the exemption from a secondary adjustment will be possible, if the following two conditions are met simultaneously:
 - a) the return is made before tax authorities decide to conduct an audit of whether the tax calculation and the tax payment are complete in connection with transactions between interdependent persons;
 - b) the taxpayer has accrued and taken into account, in determining the tax base for corporate income tax, income in the form of interest for the use of its counterparty's funds for each day of use of funds until the date immediately preceding the day of return of income. The interest is calculated at a rate of 1/300 of the key rate of the Central Bank of Russia in effect on the day on which the excess income is paid.

We recommend carefully documenting the grounds and the actual return of income for the purposes of exemption from secondary adjustments and complying with applicable Russian currency laws.

4. INFORMATION SOURCES LIMITED

The Russian Tax Code contained a rule allowing the taxpayer to use “any publicly available sources of information” to substantiate the arm’s length nature of transfer prices. This rule confirmed that the list of information sources that a taxpayer could use was open-ended. Now, however, the Russian legislature has proposed to limit the list of information sources to those explicitly listed in Article 105.6 of the Russian Tax Code [9]. Although this article contains a broad list of sources, which would in practice be sufficient for most situations, we believe that the restrictive approach proposed by the Russian legislature itself is erroneous.

On the other hand, the prohibition on tax authorities using other information has been lifted if they have information about the taxpayer's internal comparable transactions [10].

A small spoonful of honey in a barrel of tar was a direct permission to use information on comparable transactions conducted by an interdependent counterparty of the taxpayer with independent persons to determine the arm’s length range. Although, in our opinion, this was allowed before without any direct reference to it in the Russian Tax Code.

9. Article 105.6(5) of the Russian Tax Code

10. Article 105.6(6) of the Russian Tax Code

5. MEDIAN VALUE OF THE RANGE

For the first time, the Russian Tax Code has introduced the concept of the median value of the arm's length /profit margin range [11]. If, after controlling transfer prices, tax authorities conclude that the applied prices do not comply with the arm's length principle, leading to an understatement of the tax base, they will use the median value of the arm's length /profit margin range to assess an additional amount of tax. Before changes were made to the Russian Tax Code, tax adjustments had been based on the boundary of the arm's length /profit margin range.

Since a calculation of the arm's length /profit margin range and the recognition of a transaction/entity as comparable is often based on the judgments of the taxpayer and tax authorities and is not of an objective nature, the determination of transfer prices by the taxpayer based on the boundary of the arm's length range will now entail a risk of additional tax assessments. Indeed, if the adjustment was made up to the boundary corrected by tax authorities before, now such an adjustment will be made up to the median value, which may imply a significant revision of transfer prices for tax purposes.

At the same time, in the case of self-adjustment, the taxpayer can still adjust its tax liabilities based on any value of the market price/profit margin within the range.

These changes facilitate the most conservative approach to pricing and motivate taxpayers to determine transfer prices based on the "central" values of the arm's length /profit margin range to minimize possible additional tax assessments.

11. Articles 105.8(4), 105.9(3), 105.10(5), 105.11(4), and 105.12(9) of the Russian Tax Code

6. USE OF QUOTATIONS AND PRICE INFORMATION AGENCIES (PIAS)

As it is known, when applying the comparable uncontrolled price method, one is permitted to use information about the price of transactions conducted on an exchange during a similar time period under comparable conditions [12]. Unlike using comparable transactions where quotations were used, the arm's length range was recognized as the range between the minimum and maximum price of transactions conducted on an exchange. This means that when building an arm's length range based on exchange quotations, it was not required to "discard" the upper and lower quartiles, as provided for building ranges based on comparable transactions. We believe that this approach was justified by the special considerations relating to trading on commodity exchanges.

Now the Russian legislature has eliminated this difference, and the arm's length range based on exchange quotations will be calculated with discarding the upper and lower quartiles, as when using comparable transactions.

Similar changes have also affected the use of data furnished by price information agencies regarding prices (price ranges) for identical (homogeneous) goods (works, services) [13].

12. Article 105.9(5) of the Russian Tax Code

13. Article 105.9(6) of the Russian Tax Code

7. TP DOCUMENTATION

The list of details to be disclosed in transfer pricing documentation has been significantly expanded. Now transfer pricing documentation must, *inter alia*, include [14]:

- 1) Income and expenses, number of employees, profit (loss), value of fixed assets and intangible assets of the foreign entity (unincorporated foreign entity) that is a party to a controlled transaction for the reporting period, in which the controlled transaction was conducted, together with supporting documents, including financial statements, if their preparation is provided for by personal law. These details must be disclosed the documentation only if the foreign counterparty is interdependent with the taxpayer.
- 2) Documents containing the registration details of the foreign entity (unincorporated foreign entity) that is a party to a controlled transaction, and details of the persons acting on behalf of that entity (unincorporated foreign entity), provided to the taxpayer at the time the controlled transaction was conducted. This information must be disclosed in transfer pricing documentation even if the counterparty is independent.
- 3) Details of the TP methods used and a functional analysis. Although these details were not formally required to be disclosed before, it has now become a mandatory component of transfer pricing documentation.
- 4) Documents confirming information about the functions of the persons who are parties to a controlled transaction, about the assets used by them, and about the economic (commercial) risks assumed by them.

It is worth noting that in practice, taxpayers have often disclosed these details and documents in their TP documentation, pursuant to the recommendations of the Russian Federal Tax Service and the OECD Guidance on Transfer Pricing Documentation. However, if the composition of information in the transfer pricing documentation could be reduced for simple and small transactions before and such information could in practice be excluded from the documentation, now this will not be possible.

14. Article 105.15(1) of the Russian Tax Code

7. TP DOCUMENTATION

Documentation is also required for some controlled transactions with independent counterparties

Before the changes in question were made, the Russian Tax Code contained a provision, whereby the requirement to provide transfer pricing documentation would not apply to transactions conducted by the taxpayer with independent persons. Although the Russian Ministry of Finance interpreted this provision as excluding the requirement to provide transfer pricing documentation only in respect of transactions with independent persons that are not recognized as controlled [15], such interpretation could hardly be considered justified. Thus, no documentation was required for uncontrolled transactions even without a special provision in the Russian Tax Code, and therefore, the interpretation of the Russian Ministry of Finance suggests that the interpreted legal text is redundant, which is inadmissible in interpretation.

Now, the Russian legislature has directly provided that it is also mandatory to submit transfer pricing documentation for transactions with independent counterparties that are equated with transactions between interdependent persons in accordance with Articles 105.14(1)(1) to 105.14(1)(3) of the Russian Tax Code [16].

15. Para. 3 of Letter No. 03-01-18/43895 of the Russian Ministry of Finance dated October 21, 2013

16. Article 105.15(2)(4) of the Russian Tax Code

7. TP DOCUMENTATION

Submission of documentation together with notice of a controlled transaction

The Russian legislature has imposed an obligation on taxpayers to submit transfer pricing documentation together with notice of controlled transactions with respect to controlled transactions in the goods included on the list of product groups specified in Article 105.14(5) of the Russian Tax Code (except for transactions between interdependent persons, the place of registration, residence, or the place of tax residence of all the parties to and the beneficiaries of which is the Russian Federation [17]). This will significantly increase the administrative burden on companies trading in these goods.

As a transitional measure, the Russian legislature has made it possible to submit documentation for transactions with these goods for 2024 at later dates—i.e., until December 1, 2025 [18].

Requesting documentation

The Russian Federal Tax Service has been given a right to request transfer pricing documentation outside the framework of an audit under Article 93.1 of the Russian Tax Code [19]. It should be remembered that Article 93.1 enables tax authorities to request documents and information regarding a specific transaction outside the framework of tax audits.

17. Article 105.15(8) of the Russian Tax Code

18. Para. 10 of Article 6 of Federal Law No. 539-FZ of November 27, 2023 On Amendments to Parts I and II of the Russian Tax Code, Certain Legislative Acts of the Russian Federation, and the Invalidation of Certain Provisions of Legislative Acts of the Russian Federation

19. Article 105.15(3) of the Russian Tax Code

8. NOTICE OF A CONTROLLED TRANSACTION

Notice of a controlled transaction may now be filed only electronically. Only individuals may still file notice on paper.

The Russian Tax Code has also expanded the scope of details to be disclosed in such a notice, by including [20]:

- 1) the terms of the transaction, and with respect to transactions in goods, the terms and basis of the delivery of the goods, the date of shipment of the goods (the date of transfer of property in the goods, the date of recognition of income (expenses) from the transaction);
- 2) the transfer pricing methods and the sources of information on comparable transactions used;
- 3) with respect to transactions between interdependent persons involving goods that are included on the list of product groups specified in Article 105.14(5) of the Russian Tax Code (except for transactions between interdependent persons, the place of registration, the place of residence, or the place of tax residence of all the parties to and the beneficiaries of which is Russia), detail of the subsequent resale transactions and/or preceding purchases of goods, including details of the end buyer, the origin of the goods, the prices, the commercial and financial terms of such transactions.

20. Articles 105.16(3)(5) to 105.16(3)(7) of the Russian Tax Code

9. MULTINATIONAL GROUP (MNE GROUP)

The Russian legislature has reconsidered its approach to the definition of a Multinational Group (MNE group). Previously, a mandatory condition for recognizing a conglomerate of entities and/or unincorporated foreign entities that were linked through equity participation or control as a multinational group would be the fact that that group had consolidated financial statements. Now, to recognize a MNE, it would be sufficient that such financial statements would be prepared if securities of any of these entities or unincorporated foreign entities were listed on a stock exchange [21]. These changes bring the Russian approach to understanding the MNE closer to the OECD approach.

The Russian legislature has imposed additional obligations on MNE groups that meet these two conditions [22]:

- 1) Over 50% of the assets of a MNE group as of the latest reporting date preceding the year, in which controlled transactions were conducted, are situated in Russia.
- 2) At least one participant in a MNE group has conducted controlled transactions in the area of foreign trade in goods included in the product groups listed in Article 105.14(5) of the Russian Tax Code.

21. Article 105.16-1(1)(1) of the Russian Tax Code

22. Article 105.16-7 of the Russian Tax Code

If a MNE meets these criteria, its parent company or an authorized participant that is a Russian entity or has declared itself a tax resident of Russia will be required to submit to the Russian Federal Tax Service information from the consolidated financial statements of that MNE, the financial statements of the members of that MNE that have conducted controlled transactions in the specified goods or facilitated those transactions (including by providing transportation, storage, packaging, insurance, financing, marketing services). This information must be supplied within 12 months after the end of the financial year, in which the transactions were conducted.

10. ADVANCED PRICING AGREEMENTS (APAS)

APA Parties

The list of taxpayers that are eligible to file an application for the formation of an advanced pricing agreement has been expanded. Thus, alongside the largest taxpayers, now taxpayers that are parties to controlled transactions involving the goods listed in Article 105.14(5) of the Russian Tax Code, with the total income (expenses) in the calendar year totaling at least RUB 2 billion will also be eligible [23].

APA Term

The Russian legislature has extended the period that can be covered by an APA. Thus, an APA can be made for the period, in which an application for the formation of a pricing agreement is submitted, plus two years before and after the end of this period [24]. The only exception is a bilateral APA with the participation of a foreign tax authority that may be made only for the year, in which the taxpayer filed an application, plus two future years.

23. Article 105.19(1) of the Russian Tax Code

24. Article 105.21(1) of the Russian Tax Code

11. LIABILITY

Now liability for non-payment or incomplete payment of tax amounts by the taxpayer as a result of the application of non-market conditions for tax purposes in controlled transactions will differ, depending on whether the transaction is domestic [25] or not.

When it comes to domestic transactions, the extent of liability will remain unchanged, as will the possibility of being exempted from liability if the taxpayer has TP documentation [26]. As for other transactions, liability will significantly increase. Thus, the penalty for such transactions will equal the unpaid tax on income recognized as dividends according to the rules for secondary adjustments, but not less than RUB 500,000.

Failure to file, or the late filing of, notice of controlled transactions will incur a penalty of RUB 100,000, rather than RUB 5,000 as was previously the case [27].

25. That is, between interdependent persons, the place of incorporation, the place of residence, or the place of tax residency of all the parties to and the beneficiaries of which is Russia.

26. Articles 129.3(1.2) and 129.3(2) of the Russian Tax Code

27. Article 129.4 of the Russian Tax Code

Failure to timely notify of participation in an MNE will incur a penalty of RUB 500,000, replacing the previous RUB 50,000 [28].

Failure to submit a Country-by-Country Report or including false information in it, and failing to submit global or national documentation, will become ten times more expensive, costing RUB 1,000,000 [29]. The same penalty will apply to failing to provide information from the consolidated financial statements of an MNE group, or a member of this group [30].

Failing to provide information about a specific MNE transaction will cost slightly less—i.e., RUB 500,000 [31].

28. Article 129.9 of the Russian Tax Code

29. Articles 129.10 and 129.11 of the Russian Tax Code

30. Article 129.11(4) of the Russian Tax Code

31. Article 129.11(3) of the Russian Tax Code

12. SAFE HARBORS

The so-called safe harbors for debt obligations have been revised—i.e., the threshold interest rates recognized as market rates that will not require additional verification of compliance with the arm's length principle. These will be the new safe harbors for debt obligations:

- In Rubles: 10% to 150% of the Central Bank of Russia's key rate, but not less than 2%.
- In Euros: 1% - STR+7%
- In Yuan: 1% - Shibor+7%
- In British pounds: 1% - SONIA+7%
- In Swiss francs: 1% - SARON+5%
- In Japanese yen: 1% - TONAR+5%
- In other currencies: 1% - SOFR USD+7%

13. APPLICABILITY

The new rules will apply to transactions, in which income or expenses are recognized for the purposes of corporate income tax starting from January 1, 2024, regardless of the date, on which the corresponding contract was entered into, unless otherwise provided by a regulation of the Russian President [32].

32. Para. 7 of Article 6 of Federal Law No. 539-FZ of November 27, 2023 On Amendments to Parts I and II of the Russian Tax Code, Certain Legislative Acts of the Russian Federation, and the Invalidation of Certain Provisions of Legislative Acts of the Russian Federation.

14. CONCLUSIONS

The amendments made to the Russian Tax Code in terms of regulating transfer pricing are likely to require taxpayers to revise their approaches to setting transfer prices, determining their market compliance, and their documentation. Given the increased liability for non-compliance with transfer pricing rules, we recommend verifying how your current approaches align with the new transfer pricing regulations. We are pleased to assist you in conducting such an audit and developing an action plan for implementing the new rules within your group of companies.

If you have any questions left or you would like to discuss something, please contact [Anton Kabakov](#).

*Best regards,
[The Forte Tax & Law Team](#)*

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