Daily Tax Report: International

New Tax Treaty Could Make Russian Companies Rethink Luxembourg

By Barbara Tasch

Aug. 12, 2020, 8:00 AM

- Russia wants higher tax rates on dividends and interest
- Hong Kong and Switzerland could be next in line

Luxembourg could become less attractive for certain investors when a renegotiated double taxation agreement with Russia comes into force.

Russia has been renegotiating its double taxation agreements with several European countries—in order to raise the withholding tax on interest and dividend payments—over the last few months. The government said Monday it aims to reach such an agreement with Luxembourg in the coming month.

If the agreement goes through on Russia's proposed terms, certain companies based in Luxembourg could reevaluate their existing structures, said Alona Gavrylova, an international tax manager at KPMG Luxembourg.

Russian groups that have companies in Luxembourg investing into Russia would most likely migrate to a jurisdiction with a "more favorable tax treaty," Gavrylova said in an email. She added that Russian companies might also go back to Russia and that the same would apply when companies choose jurisdiction for future structuring.

Furthermore, Luxembourg companies that invest into Russia would need to reassess "the effectiveness of existing ownership structures of Russian assets," Gavrylova said. Joint ventures established in Luxembourg by Russian groups and foreign investors, in addition to Luxembourg banks that grant loans to Russian companies could also be affected, she said.

Under Russia's proposed terms, the renegotiation would raise the minimum withholding tax rate on dividend payments from 5% to 15% and on interest payments from 0% to 15%. Cyprus agreed to a similar renegotiation with Russia on Monday.

Alexey Sazanov, deputy finance minister said in a statement that the Russian finance ministry will conclude negotiations with Luxembourg and Malta in the coming month and that both countries had generally agreed with the proposed terms.

Luxembourg's finance ministry declined to comment on the matter. The Maltese government confirmed in an email that Malta and Russia "agreed to negotiate new terms concerning the tax treaty between the two jurisdictions."

Steven Koener, an international affairs advisor at the Luxembourg Chamber of Commerce, said that it is important the agreement is signed soon to bring certainty to companies in Luxembourg.

"Any decision will be better than the limbo of what's going to change," Koener said. Uncertainty "won't allow any company to plan long term," he said. A new deal would have an impact on Luxembourg-based companies with investments or activities in Russia, he added.

After threatening to unilaterally pull out of its double taxation agreement with Cyprus, Russia announced earlier this week it had found an agreement with the island nation. Russia's Deputy Prime Minister Oleksiy Overchuk said Cyprus "fully agreed" with Russia's proposals.

Russia announced Tuesday it might also amend its double tax treaties with Hong Kong and Switzerland. It wants to change its treaty with the Netherlands, as well.

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