

MEMORANDUM OF UNDERSTANDING

A Finnish delegation and a Russian delegation met in Moscow, at the Ministry of Finance, on 9 November 2004 to discuss certain issues related to the interpretation and application of the Agreement between the Government of the Republic of Finland and the Government of the Russian Federation for the avoidance of double taxation with respect to taxes on income, signed at Helsinki on 4 May 1996, as amended by a Protocol signed at Helsinki on 14 April 2000 (hereinafter referred to as "the Agreement").

The Finnish delegation was headed by Mr. Antero Toivainen, Director for International Tax Affairs, Ministry of Finance, while the Russian delegation was headed by Mr. Dmitry Nikolaev, Head of International Taxation Division. The list of both delegations is attached as Annex I.

The discussions resulted in the following common understanding on the issues dealt with:

1. With reference to Article 5, Article 7 and Article 8 of the Agreement

International traffic

Article 8 is an exception to Article 7, that is, the income subject to Article 8 cannot be taxed in a Contracting State although there is a permanent establishment in that State. The aim of Article 8 is to exempt income from international traffic from the source country taxation. If the activity is covered by Article 8, the question whether there is a permanent establishment, is of no relevance. If a transport business activity is not covered by Article 8, Article 7, together with Article 5, must be applied.

According to Article 8 paragraph 2: "Profits or income of a resident of a Contracting State from the use, maintenance or rental of containers (including trailers, barges and related equipment for the transport of containers) used for the transport of goods or merchandise shall be taxable only in that State, except where such containers are used for the transport of goods or merchandise solely between places within the other Contracting State." The expression "container" signifies a means of transportation used for the transportation of goods and "the profits or income from the use, maintenance or rental" signifies for example income from letting of such a container by an enterprise of a Contracting State shall be taxable only in that State.

2. With reference to Article 5, paragraph 3 of the Agreement

The determination of whether to consecutive building sites etc. form one permanent establishment

When determining whether consecutive building sites form one permanent establishment the following principles must be taken into account:

The time limit test applies to each individual site or project. In determining how long the site or project has existed, no account should be taken of the time previously spent by the contractor concerned on other sites or projects which are totally unconnected with it. A building site should be regarded as a single unit, even if it is based on several contracts, provided that it forms a coherent whole commercially and

geographically. Subject to this proviso, a building site forms a single unit even if the orders have been placed by several persons (e.g. for a row of houses).

3. With reference to Article 5, paragraph 3 of the Agreement

Where the factual duration of a building site exceeds the time limit of 12/18 months that building site etc. is deemed to be a permanent establishment from the very start of its existence. Accordingly, the provisions of Article 7 concerning the right to tax profits of a permanent establishment shall be applicable from that date.

4. With reference of Article II of the Protocol signed at Helsinki 14 April 2000 and taking into account that the Agreement is applicable from 1st January 2003

Transitional period for a building site etc.

In the case of enterprises

If the period of a building site etc. which an enterprise of a Contracting State has in the other Contracting State has been started before 1st January 2003 exceeds 36 months after that date, a permanent establishment is deemed to exist only for that part of the period which has started on or after 1st January 2003. Accordingly, the provisions of Article 7 concerning the right to tax profits of a permanent establishment shall be applicable from 1st January 2003. Correspondingly the provisions of paragraph 3 of Article 7 shall be applicable to expenses of such a permanent establishment.

Example I: If an enterprise has started such building site etc. on 1st December 2002 and its activities have lasted for 37 months to 31st December 2005, only December 2002 is time when a permanent establishment has not existed and thus tax exempt. Accordingly, the provisions of Article 7 concerning the right to tax profits of that permanent establishment shall be applicable from 1st January 2003. Correspondingly the provisions of paragraph 3 of Article 7 shall be applicable to expenses of such a permanent establishment.

Example II: If an enterprise has started such building site etc. on 1st June 2001 and its activities have lasted for 37 months to 30th June 2004, only the period from 1st June 2001 to 31st December 2002 is time when a permanent establishment has not existed and thus tax exempt. Accordingly, the provisions of Article 7 concerning the right to tax profits of that permanent establishment shall be applicable from 1st January 2003. Correspondingly the provisions of paragraph 3 of Article 7 shall be applicable to expenses of such a permanent establishment.

In the case of personnel of a building site etc.

When the period of a building site etc. which an enterprise of a Contracting State has in the other Contracting State has been started before 1st January 2003 exceeds 36 months after that date, remuneration derived by an individual referred to in subparagraph a) of paragraph 2 of Article 11 of the Agreement between the Government of the Republic of Finland and the Government of the Union of Soviet Socialist Republics for the avoidance of double taxation with respect to taxes on income, signed at Moscow on 6 October 1987, shall be taxable only for the period exceeding 36 months in the Contracting State where the employment is exercised.

Example: An enterprise of a Contracting State has started its building site etc. in the other Contracting State on 1st December 2002 and its activities have lasted for 37 months to 31st December 2005. Only the remuneration for December 2005 is taxable in the other Contracting State where the employment is exercised.

5. With reference of Article II of the Protocol signed at Helsinki 14 April 2000

Possibility to extend the 36 months' period.

The delegations noted that on the basis of Article II of the Protocol signed at Helsinki 14 April 2000 there is a possibility to apply for an extension of the 36 months' period concerning a building site etc. in exceptional cases.

Done at Moscow on 9 November 2004, in duplicate, in English language, both texts being equally authentic.

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