Double Tax Relief - Tax Treaties

2021

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Content

A. General Comments on Treaties

Objective of Tax Treaties:

- Prevent double taxation of the same income in different states
- State of residency may not grant sufficient relief
- Allocation of right of income
- Pushing domestic economy

Relation between domestic law and treaties:

-Treaty needs to be transposed into national law
-Some jurisdictions allow "treaty overrides" (case pending at German Constitutional Court)
-Treaty can only restrict national law, not enhance domestic tax rules; treaty relieve may result in double non-taxation. More modern treaties try to avoid double non-taxation.
-Protocols are part of the treaty

Model Treaties

- OECD Model Treaty
- UN Model Treaty
- US Model Treaty

Interpretation of Treaties:

Sources of interpretation Definitions in the Treaty:

-Commentary OECD Model Treaty
-National law of applying state

Anti – abuse provisions

- All states apply anti-abuse provisions with regard to treaty benefits.

Treaty itself may contain anti-abuse provisions (e.g. Limitation of Benefits Clause in Treaty USA-D).

- Domestic law may provide for a special anti treaty shopping provision
- General anti-abuse provision under domestic law may apply

B. Contents of a typical Tax Treaty

- Scope of treaty (income tax, inheritance/gift tax)
- Definitions
- Allocation of income
- Avoidance system (exemption method (with progression) / credit method)
- Special (procedural) provisions (e.g. exchange of information)

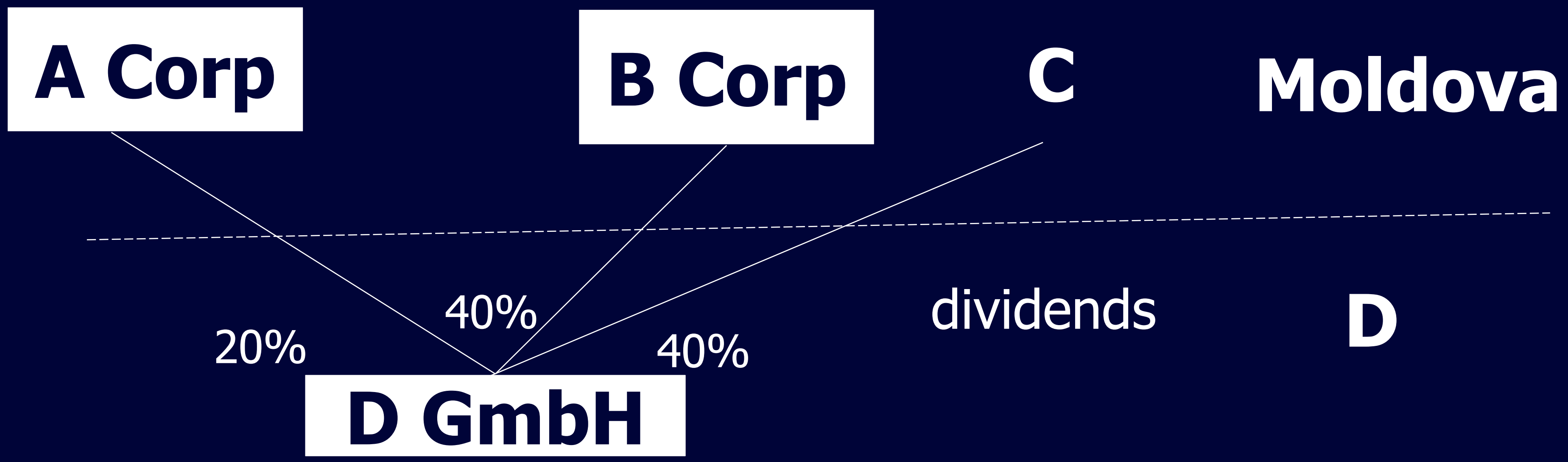
C. Relevant Treaty Provisions

Art. 6: Income from immovable property
• Source state has unlimited right of taxation

Art. 7: Business profits
Source state has no right of taxation, unless the income can be attributed to a permanent establishment.
Permanent Establishment (Art. 5): Fixed place of business
Place of effective Management
Dependent agent with right to enter into binding contracts for the principal

Art. 10: Dividends
• Source state has limited right of taxation 5% of gross dividends if shareholder is corporation holding directly at least 25% of the shares in the distributing entity.
• 15% in all other cases.
• State of residency grants tax credit.
• Source state has unlimited right of taxation if dividends can be attributed to PE of the company in the source state.

Art. 10: Dividends
The right of source state to withhold taxes depends on shareholder and participations rates.



Art. 11: Interest
• Source state has limited right of taxation: 10%* of gross interest.
• State of residency grants tax credit.
• Source state has unlimited right of taxation if interest can be attributed to PE of the company in the source state.
• If interest expenses can be attributed to a PE this state is regarded to be the source state.

Art. 12: Royalties
• Source state has no right of taxation.
• Source state has unlimited right of taxation if interest can be attributed to PE of the company in the source state.

Art. 13: Capital gains
Source state has no right of taxation, unless asset can be attributed to a PE in the source state
asset is real estate
shares in a real estate company

Art. 15: Income from employment
• State where the employee exercises her/his activity (source state) has the right of taxation, unless the employee is in this state for less than 183 days and
• no remuneration is paid by or on behalf of the employer resident in the source state and
• the remuneration can not be attributed to a PE of the employer in the source state.

D. Typical Treaty Problems

Residency of individuals

• Treaty grants benefits to residents (within the meaning of the treaty) only

• An individual is resident in a state if she/he is taxed by this state due to her/his residency (i.e. is subject to unlimited taxation).

• Residency generally mean place to live

• A person can be resident in several states according to the relevant domestic law.

• In such case tie breaker rule applies, generally "centre of vital interests" is decisive.

Residency of corporations

• Treaty grants benefits to resident corporations only

• A corporations is resident in a state if it is taxed by this state due to its residency (i.e. is subject to unlimited taxation).

• Residency under domestic law generally mean place of statutory seat or place of effective management

• A corporation can be resident in two states according to the relevant domestic law.

• In such case tie breaker rule applies, place of effective management is decisive.

Residency of partnerships

• Some jurisdictions treat partnerships like corporations. Some jurisdicitions treat partnerships as transparent entities. Can partnerships rely upon treaty benefits?

E. How are double tax treaties implemented in Moldova?

- Moldova is usually using the credit method to avoid double taxation.
According to it, the incomes of a company with foreign participation are taxed in Moldova and the resident country is offering a refund for the amount.

- An important fact related to this method is that the claimed amount of money cannot be higher than the amount that could have been resulted after taxing the same amount of income in the resident country.

	Moldova	Germany
Taxable Income	100.000	10.000
All kind of Taxes	(40%) 40.000	(30%) 3.000
Taxes on foreign source income	4.000	
Taxes credited	3.000	
Taxes to be paid	37.000	

F. Moldova has 50 operational DTTs

Recipient/Year into force	WHT * (%)		
	Dividends	Interest	Royalties
Non-treaty	6/15 **	12	12
Treaty:			
Albania (2003)	5/10	5	10
Armenia (2005)	5/15	10	10
Austria (2005)	5/15	5	5
Azerbaijan (1999)	8/15	10	10
Belarus (1996)	15	10	15
Belgium (1996)	15	15	0
Bosnia and Herzegovina (2004)	5/10	10	10
Bulgaria (1999)	5/15	10	10
Canada (2002)	5/15	10	10
China (2001)	5/10	10	10
Croatia (2006)	5/10	5	10
Cyprus (2008)	5/10	5	5

Double Tax Treaties Signed with Moldova

Czech Republic (2000)	5/15	5	10
Estonia (1998)	10	10	10
Finland (2008)	5/15	5	3/7
Georgia (2019)	5	5	5
Germany (1995)	15	5	0
Greece (2005)	5/15	10	8
Hungary (1996)	5/15	10	0
Ireland (2010)	5/10	5	5
Israel (2007)	5/10	5	5
Italy (2011)	5/15	5	5
Japan (1998)	15	10	0/10
Kazakhstan (2002)	10/15	10	10
Kuwait (2013)	0/5	2	10
Kyrgyzstan (2006)	5/15	10	10
Latvia (1998)	10	10	10
Lithuania (1998)	10	10	10
Luxembourg (2009)	5/10	5	5
Macedonia (2006)	5/10	5	10
Malta (2015)	5	5	5
Montenegro (2006)	5/15	10	10
The Netherlands (2001)	0/5/15	5	2

Double Tax Treaties Signed with Moldova

Oman (2007)	5	5	10
Poland (1995)	5/15	10	10
Portugal (2010)	5/10	10	8
Romania (1996)	10	10	10/15
Russian Federation (1997)	10	0	10
Serbia (2006)	5/15	10	10
Slovakia (2006)	5/15	10	10
Slovenia (2006)	5/10	5	5
Spain (2009)	0/5/10	5	8
Switzerland (2000)	5/15	10	0
Tajikistan (2004)	5/10	5	10
Turkey (2000)	10/15	10	10
Turkmenistan (2013)	10	10	10
Ukraine 1996)	5/15	10	10
United Arab Emirates (2018)	5	6	6
United Kingdom (2001)	0/5/10	0/5	5
Uzbekistan (1995)	5/15	10	15

* If multiple rates are listed, then the WHT rate to be applied is subject to fulfilment of specific criteria provided by the DTT.
** 15% on dividends referring to the profit earned incurred during the period 2008 to 2011.

G. Tax information exchange

- ✓ Moldova has also signed tax information exchange agreements.
- ✓ According to these treaties, Moldova must provide lists with the taxpayers to the willing partners and also receive this type of information from its partners.
- ✓ This way, the entrepreneurs wanting to take advantage of the double tax treaties regulations and not paying any taxes in Moldova and abroad are discouraged.
- ✓ If an entity wants to claim a refund, he must bring a certificate of residence in another country and a proof that the taxes are already paid there (usually where the business takes place).

H. Taxation in Moldova:

- **Currency –** Moldovan Leu (MDL)
- **Foreign exchange control –** *Resident and nonresident legal entities are obliged to make and receive payments and transfers involving foreign currency operations through their bank accounts. There are certain limitations on when such entities may use cash or payment instruments to perform foreign currency operations.*
- **Accounting principles/financial statements –** *IFRS are mandatory for entities of public interest (i.e. entities traded on a regulated market, banks, (re)insurance companies, collective investment funds, state-owned enterprises or joint stock companies that are more than 50% state-owned. Other companies may apply IFRS or National Accounting Standards (NAS).*
- **Principal business entities –** *These are the limited liability company, joint stock company, partnership, sole proprietorship, branch and representative office of a foreign corporation.*

I. Corporate taxation:

- **Residence –** *A corporation is resident if it is established or managed in Moldova.*
- **Basis –** *Residents are taxed on their worldwide income; nonresidents are taxed only on income derived from certain Moldovan sources.*
- **Taxable income –** *Taxable income is based on the accounting income for the year as adjusted for tax purposes for items specifically provided by the Tax Code.*
- **Taxation of dividends –** *Dividends received by a Moldovan resident company from another Moldovan company are not taxed at the level of the recipient.*
- **Capital gains –** *Capital gains of companies are taxed as ordinary income, but only 20% of the gain is taxable.*

- **Losses –** *Corporate tax losses may be carried forward for five years. The carryback of losses is not permitted.*
- ***Rate*** **–** *12%. However, business entities not registered as VAT payers (except farmers, individual entrepreneurs, and entities providing business and management consulting services), may calculate income tax by applying a 4% rate to their operating income.*
- **Surtax –** *No*
- **Alternative minimum tax –** *No*
- **Foreign tax credit –** Resident taxpayers are entitled to a tax credit for the tax paid on foreign income. The credit is limited to the amount of Moldovan tax that would have been imposed on the foreign profits.
- **Participation exemption –** *No*
- **Holding company regime –** *No*
- **Incentives –** *Tax incentives are available for farmers, entities operating from information technology parks, business entities that increase the number of employees and those operating in free economic zones.*

J. Withholding tax:

- **Dividends –** *Dividends paid by Moldovan resident companies to both residents and nonresidents are subject to a 6% tax, unless the rate is reduced under an applicable tax treaty.*
- **Interest –** *Interest paid to a nonresident is subject to a 12% withholding tax, unless the rate is reduced under a tax treaty.*
- **Royalties –** *Royalties paid to resident individuals and nonresidents are subject to a 12% tax, unless the rate is reduced under a tax treaty.*
- **Technical service fees –** *Service fees paid to nonresidents are subject to a 12% withholding tax, unless the rate is reduced under a tax treaty.*
- **Branch remittance tax –** *No*

K. Other taxes on corporation:

- **Capital duty –** No
- **Health insurance contribution** - *until now, the employee paid 4.5% for the medical insurance, but as of January 1, 2021 the employee pays the full health insurance. Instead, the employer assumes the responsibility for the full payment of the contribution to the pension fund (see below).*
- **Pension fund contribution** – *until now, the employee paid 6% of the salary for the pension fund, but starting with January 1, 2021 the social insurance contribution calculated to the amount of salaries and rewards is due in total amount by the employer.*
- Thus, if until now the employee paid 6% of the salary for the pension fund and 4.5% for the medical insurance, which constituted a total of 10.5%, from January 1, 2021 the employee will pay only the full medical insurance, ie 9% from income. The above-mentioned changes will contribute to the simplification of the procedure for calculating and paying the respective contributions for the employer and to the optimization of the payment administration process. Regarding the impact of the changes on the insured persons employed, the amount of payments incurred will decrease by 1.5%.

- **Real property tax –** *Residents and nonresidents that own immovable property in Moldova must pay real property tax at rates set annually by the local public administration authority. The rate may not be less than 50% of the maximum rate stipulated by the law.*
- **Stamp duty –** *Stamp duty may apply on claims submitted to the court of justice, registration of mortgages, notary acts, etc.*
- **Transfer tax –** *Transfer taxes are charged upon notary authentication of transactions related to the transfer of property. The tax ranges from 0.1% to 1.3%, applied to the value of the transaction.*

L. Anti-avoidance rules:

- **Transfer pricing –** *There is no specific transfer pricing legislation in Moldova, although the tax code provides that the arm's length principle should be applied to transactions with related parties. Losses incurred on transactions between related parties are not deductible for corporate tax purposes.*
- **Thin capitalization –** *The deduction of interest on borrowings received from individuals and legal entities, other than financial institutions, micro-financing organizations and leasing companies is allowed only within the limit of the average weighted rate set by the National Bank of Moldova for loans granted by the banking sector to legal entities.*
- **Controlled foreign companies –** *No*
- **Disclosure requirements –** *No*

M. Compliance for corporations:

- **Tax year –** *Calendar year. For a new company, the tax year is the period from the date of registration until the end of the calendar year. A company that is a member of a multinational group may apply a different period that corresponds to its financial reporting period, provided the tax authority is notified in advance*.
- **Consolidated returns –** *Consolidated returns are not permitted; each company must file its own return.*
- **Filing requirements –** *Moldova operates a self- assessment regime. The tax return must be submitted by the 25th day of the third month following the end of the tax year.*
- **Penalties –** *Penalties apply for late filing, failure to file and tax avoidance/evasion.*
- **Rulings –** *The taxpayer may request "comfort letters" from the tax authorities. Comfort letters are submitted to taxpayers free of charge. Advance individual tax rulings may also be requested from the tax authorities. The deadline for issuance is 90 days from the date of submission of the request to the tax authorities. The fee for issuing an advance individual tax ruling is MDL 60,000 for large taxpayers and MDL 30,000 for other categories of taxpayers.*

N. Personal taxation:

- **Basis –** *Resident individuals, both Moldovan citizens and foreigners, are taxed on their income related to activities performed in Moldova. Moldovan citizens also are taxed on financial income and investment income obtained from sources outside Moldova. Nonresidents are taxed only on their Moldovan-source income.*
- **Residence –** *An individual is resident if he/she is domiciled in Moldova or present in Moldova for more than 183 days during the tax year.*
- **Filing status –** *Each individual who has an obligation to pay income tax must file a return; joint returns are not permitted.*
- **Taxable income –** *Taxable income represents the gross income obtained from all sources during the tax period, reduced by the deductions and allowances permitted by law. Gross income includes, but is not limited to, salary/wages, benefits, capital gains, rents, royalties and annuities.*

- **Capital gains –** *Capital gains of individuals are treated as ordinary income, but only 20% of the gain is taxable. The capital gain on the disposal of a private residence where the taxpayer has lived and that was owned by the taxpayer for at least three years before the disposal is tax exempt.*
- **Deductions and allowances –** *Personal allowances are available to the taxpayer and his/her spouse, children and dependents. Deductions are granted for medical insurance and individual social security contributions.*
- **Rates –** *12%*
- **Other –** *Resident individuals carrying out trade activities without being organized under a legal form and whose annual income from those activities does not exceed MDL 600,000, are liable to tax of 1% (subject to a minimum charge of MDL 3,000).*

O. Other taxes on individuals:

- **Capital duty –** *No*
- **Stamp duty –** *Stamp duty may apply to the registration of civil status documents of domicile, of mortgages, for notary acts, etc.*
- **Capital acquisitions tax –** *No*
- **Real property tax –** *Residents and nonresidents that own immovable property in Moldova must pay real property tax at rates set annually by the local public administration authority. The rate may not be less than 50% of the maximum rate stipulated by the law.*
- **Inheritance/estate tax –** *No*
- **Net wealth/net worth tax –** *A wealth tax is applied to individuals who own real estate in Moldova (except for land), with an estimated value of at least MDL 1.5 million and an area of at least 120 square meters. The wealth tax is charged at 0.8% on the value of the real estate and the tax must be paid by 25 December during the tax period.*
- **Social security –** *Employees must contribute to the social security fund an amount equal to 6% of their gross salary. Employees also must make health insurance contributions at 4.5% of gross salary. The contributions are deductible for income tax purposes.*

P. Compliance for individuals:

- **Tax year –** *Calendar year*

- **Filing and payment –** *The deadline for filing personal income tax returns and payment of the tax due is 30 April of the subsequent fiscal year. For salary income, the employer withholds tax on behalf of the employee and files monthly tax reports.*

- **Penalties –** *Penalties apply for late filing, failure to file and/or tax avoidance/evasion.*

Q. Value added tax:

- **Taxable transactions –** *VAT is levied on the supply of goods, the provision of services and the import of goods and services into Moldova.*
- **Rates –** *The standard rate is 20%. A reduced rate of 8% applies to certain food products; drugs; biofuels used for electricity, heating and hot water production; and specific phytotechnical, horticultural and zootechnical products. International transportation and exports are exempt with credit. Certain items (financial services, postal services, cars, land and dwellings, etc.) are VAT exempt with no right to deduct.*
- **Registration –** *Registration for VAT purposes is mandatory when a business entity carries out taxable supplies and imports VAT-taxable services in excess of MDL 1.2 million during a consecutive 12-month period. A business entity may apply for voluntary registration if it plans to carry out VAT-taxable supplies.*
- **Filing and payment –** *VAT payers must prepare and submit VAT returns on a monthly basis. The filing and payment of VAT must be carried out no later than the 25th day of the following month. VAT related to imported services must be paid on the date the service is paid for, and VAT on imported goods must be paid before the goods clear customs.*

EXPERIENCE

MOLDOVA

- Our tax advisers have 20 years of substantial experience in Taxation matters, providing advice on structuring in a wide range of corporate and financial transactions, in order to achieve maximum tax benefits, leading to efficiency and optimization in all types of businesses, both in terms of direct taxation and in terms of VAT.

- The team also holds a broad expertise in International Taxation, especialy:

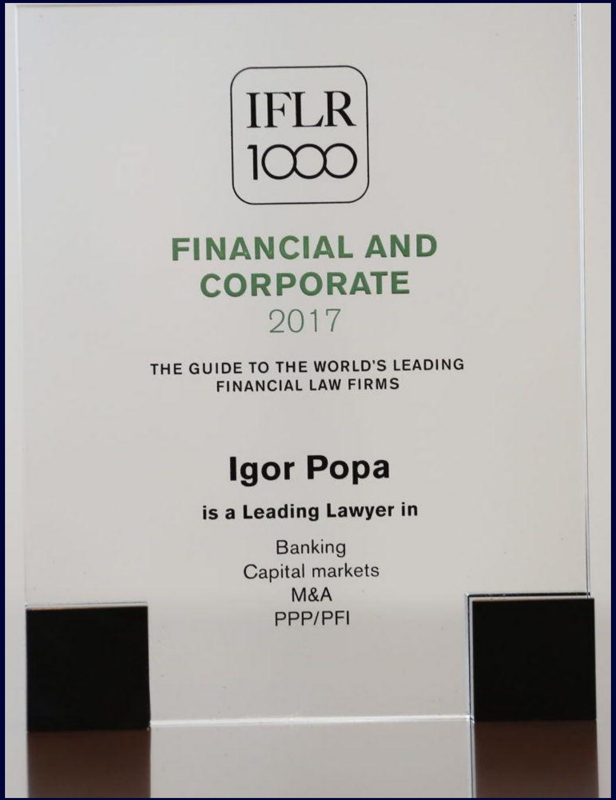
  • Avoiding double taxation

- • Minimization of global tax risks

- • Sustainable Tax planning rather than taking advantage of short-term "loopholes"

- GRATA Moldova combine knowledge and experience from our Senior Partner Igor Popa with Accounting / IFRS background and to achieve the wider benefits that an effective tax planing to the new standards can bring.

AWARDS



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