

AN OVERVIEW OF NORMATIVE DOCUMENTS ON TAXATION ISSUES FOR MARCH–APRIL 2014

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The most noteworthy developments over the period under consideration, against the backdrop of ever growing economic sanctions being imposed by the West and the resulting capital outflow from Russia, are the assertion, by Russian authorities, of lack of any intention on their part to further increase the tax burden, as well as the measures suggested by the RF Ministry of Finance for the purpose of further de-offshorization of Russia's economy, as well as measures designed to increase the economic responsibility of Russian organizations acting as tax agents responsible for proper transfer of dividends and interest due to foreign investors on the basis of tax exemption mechanism in those instances when the said foreign investors are not identified in accordance with Russian legislation as genuine beneficiaries (owners) of such incomes¹.

We believe that these measures alone will be insufficient for doing away with stagnation in Russia's economy. The core of the matter is that the measures considered to be necessary for overcoming the stagnation trend – no matter what its actual cause has been in the first place, a generally unfavorable economic situation or some specific political developments, – should be those aiming at reducing the tax burden on commodity producers, implemented in conjunction with some provisional measures designed to bring down the level of government expenditure. As long as businesses are properly functioning, they create demand for workforce and form an independent market, while the government, by cutting its expenditures, reduces the demand for tax-generated revenues and, consequently, the tax burden. However, if the aggregate tax burden is not reduced, and government expenditures, instead of being reduced, undergo a simple change of their structure (a shift toward government investment), the negative trend in economic development will, regretfully, by no means be reversed.

De-offshorization will not provide any adequate solutions to the existing problems, either – given the continuing decline of the economic development rate: if capital flees the country and is not going to return, Russian corporate tax agents will not be able to find sources to compensate for their losses incurred as a result of toughening of their tax obligations, and so they will rapidly lose their investors and be forced to shut down.

It would be technically easier to cut government expenditures in conditions of depreciation of the national currency, but the money thus saved will probably be spent on fulfilling the RF President's pre-election promises to raise pensions, salaries and increase other social expenditures; in fact, this means that the savings created as a result of declining real incomes of some population groups will be used to cover the consumer spending by other groups, namely to support imports in order to improve the current consumption level of socially vulnerable population strata. In any event, Chairman of the RF Government Dmitry Medvedev, when reporting to the State Duma the results achieved by his government in 2013, spoke of the necessity to fulfill all the previously assumed social obligations². It should be added though, that the government's chairman also mentioned the plan to cut by 10% the number of Russian government officials both at the regional and federal levels, in addition to the previously announced 20% cut. However, in reality this will hardly result in any true reduction in the amount of government expenditures.

According to the RF Ministry of Finance, the main ways to sustain the revenue base of Russia's budgets in the present situation will be to reduce the number of tax exemptions (the Ministry estimates that the losses of the federal and regional budgets resulting from tax exemptions have amounted to Rb 2 trillion³, and so now it is prepared to grant to regional authorities the right to abolish the exemptions from regional and local taxes introduced at the federal level), and also to switch over to cadastre-based valuation of the tax base for

1 A. Shtykina, Minfin sostavil instruktsiiu po presecheniiu vyvoda pribyli v ofshory [The RF Ministry of Finance has elaborated instructions for preventing profit outflow to offshore zones]. See top.rbc.ru/economics/22/04/2014/919508.shtml; Plan-perekhvat nalogov. Rosfinmonitoring gotovitsia proverit' benefitsiarov [The Tax Interception Plan. Rosfinmonitoring [Federal Financial Monitoring Service] is preparing to check on the beneficiaries]. See kommersant.ru/doc/2444518.

2 Dmitry Medvedev promised that any dramatic turnarounds in the economy will be avoided. See top.rbc.ru/politics/22/04/2014/919615.shtml.

3 A. Kiselev. Moratorii nuzhno vvesti ne tol'ko na l'goty, no i na vse drugie elementa naloga [A Moratorium Must Be Imposed Not Only on Tax Exemptions, But Also on Other Components of the Tax]. See kommersant.ru/doc/2453151, 15 April 2014.

the tax on immovable property transferred to regional and local budgets (it should be mentioned in this connection that the RF Government has recommended to the regions that they must not forcibly speed up this process). Besides, the RF Ministry of Finance has also somewhat softened (falling short of completely eliminating them) the financial risks created for the banking system by the economic sanctions introduced against Russia. In connection with the suspension, at the intergovernmental level, of the negotiations concerning the Russian Federation's signing on to FATCA¹, the RF Ministry of Finance developed alterations to RF legislation whereby Russian banks will be allowed to directly deal with US tax agencies (US IRS²) in the FATCA framework³. However, until 1 January 2015 Russian banks will not be obliged to operate as tax agents for the IRS – that is, withhold and transfer to the US budget 30% of the monies received in the accounts of US residents opened with those banks (so far, the banks will only be collecting information on their clients). But if the issue as to recognizing Russian banks as enrolled tax agents by the US IRS is not properly regulated prior to the year-end of 2014, sanctions may be imposed on Russian banks in the form of suspension of their operations or closure of their correspondent accounts with Western banks.

The worsening prospects for Russia's economic development have also triggered a search in the business community for some mechanisms that can help prevent any further progress in the negative trends. According to President of the Russian Union of Industrialists and Entrepreneurs (RSPP) Alexander Shokhin, Russia is currently at a crossroads – 'The mobilization model for the economy, or a radical improvement of the business climate'. He suggested that the business community should stand for the latter scenario at the

1 FATCA (Foreign Account Tax Compliance Act) is a US tax law whereby non-resident banks are required to submit to the US Internal Revenue Service information on the operations carried on in the accounts opened with those banks by US residents and the persons controlled by those US residents, and to act as tax agents with regard to operations involving the handling of income derived from sources in the USA, to the extent of closing the accounts of non-complying clients.

2 Internal Revenue Service.

3 O. Shestopal, *Minfin nashel vkhod v FATCA. Rossiskim bankam propisali pravila raboty s SShA* [The RF Ministry of Finance Has Found an Entrance to FATCA. Russian Banks Have Been Prescribed Rules for Working with the USA]. See kommersant.ru/doc/2449026 of 10 April 2014. 'The alterations to Russian legislation have allowed banks not only to directly inform the IRS on the accounts and operations of US taxpayers in Russia without violating thereby Russian legislation, but also to close the accounts of those of them who avoids disclosing that information. However, as before, Russian banks will not be able to act as tax agents before the IRS, which means that they still be faced with the related risks – those of their correspondent accounts abroad being closed'.

public reading of Business Ombudsman Boris Titov's report at the International Economic Forum in St. Petersburg in June⁴.

The well-known businessman and ex-leader of the *Civic Platform* party Mikhail Prokhorov put forth his own solutions in the framework of his comprehensive program for Russia's development⁵. These solutions are clearly oriented to the interests of big businesses, and so they should be treated with caution. It is indeed possible that free access to hydrocarbon extraction granted, as he suggests, to private entrepreneurs may result in increasing output and lowering extraction costs. However, the demand on world raw materials markets has for a long time already been regulated through the use of production and supply quotas, in order to maintain a stable level of world prices. In reality, free access of private capital to hydrocarbon extraction may only result in replacement of the key players in that market segment, with little effect to the national economy at large. As for the proposal that land should no longer be divided into categories in accordance with its uses (agricultural land, land for housing development projects) and instead be placed on the market for free and unlimited circulation, it must be remembered that land and subsoil alike are legislatively consolidated in joint ownership by the Federation and the Federation's subjects, and represent the same type of natural monopoly as natural mineral resources. A free commercial turnover of land can hardly be possible under a federative multi-national state system. In this sphere, there will always be a hierarchy of relationships at several levels: the Federation and a Federation's subject; a Federation's subject and the owner of a land plot. Land resources, similar to other natural resources, are subject to physical limits – that is, they constitute a state natural monopoly. A state natural monopoly is a special type of monopoly, it is based on every citizen's right to enjoy the welfare produced by such a monopoly, and the government's role (or function) – that is, the government's service – consists in most efficiently governing that natural monopoly for the benefit of entire society. Natural monopoly, in our opinion, must be distinguished from other types of state monopoly, the creation of the lat-

4 V. Khamraev, *Nas malo i nas vse men'she. Buzines-ombudsman Boris Titov gotovit doklad dlia prezidenta* [There are Few of Us, and We Are Becoming Fewer Still. Business Ombudsman Boris Titov Is Preparing a Report for the President]. See kommersant.ru/doc/2453139 15 April 2014.

5 NEP 2.0: *ob oborone i nastuplenii* [NEP 2.0: On Defense and Offensive]. See kommersant.ru/doc/2453979. Mikhail Prokhorov: 'First, to launch a wave of private housing construction around big cities. For this to be done, land use categories must be abolished, and a mass of new land plots must be thrown on the free market, in order to radically reduce prices'.

ter oftentimes being motivated by factors other than economic and involving a ban of restrictions on certain activities (for example, a ban imposed by local authorities on free parking in a city center, or the numerous types of mandatory licenses granted by government agencies for the right to render certain services¹). An optimization of the list of paid government services may indeed help in eliminating these unnecessary state monopolies. But Prokhorov's proposals envisage lifting of any restrictions specifically on the natural monopolies market. But absence of restrictions on the circulation of natural resources may give rise to controversial consequences, and in any event it is unlikely that this measure may indeed promote innovation development of the economy.

The issues of economic stagnation in Russia and the need to put an end to it have also stirred a stronger interest in the comprehensive package of technical measures suggested by the International Monetary Fund (IMF) for dealing with the current financial instability Ukraine in the framework of the preliminary arrangement, announced on 28 March 2014, for a \$ 14–18bn stand-by loan agreement. The aim of the suggested measures: 'to try to immediately eliminate two big disbalances: fiscal and external'².

The 'technology' for exiting the crisis suggested by the IMF to Ukraine relies in the main on eliminating the external disbalance through depreciation of the national currency. When a national currency loses its value against world currencies, imports shrink (and so less currency is spent), and the conditions improve for exports (the equivalent of proceeds from exported product denominated in world currencies increased the amount of exporter profit denominated in the national currency, thus boosting production efficiency).

A similar policy is currently being pursued by the RF Central Bank – the ruble's free floating coupled with a high key rate of refinancing, to cut off speculative market demand for ruble-denominated funds with the purpose of converting them into world currencies. All these measures are designed to ensure priority development of export-oriented non-raw-materials industries. The IMF experts have pointed out in connection with the situation in Ukraine that a country with

a considerable deficit in its foreign trade and current operations accounts must have definitely made some mistakes in planning its exchange rate policy. Evidently, this consideration is no news for Russian authorities, either. It is not a coincidence that the RF President, in his conversations during *Direct Line with Vladimir Putin* on 17 April 2014, confirmed the RF government's intent to stick to the budgetary rule, whereby the amount of oil proceeds gained in excess of planned budget oil price targets is earmarked for government reserve funds – even in face of a plummeting growth rate in the Russian economy³. By doing so, Russian authorities are trying to eliminate the effects of the raw materials factor on the processes of allocation of funding to cover government expenditures. This should be regarded as the manifestation of an efficient economic policy, provided that, at the same time, some mechanisms will be created for an active involvement of private businesses in structural changes in the national economy. Ukraine and Russia are faced with somewhat similar problems in their post-Soviet economies, and so the methods applied in the attempts to improve the economic situation in those two countries can be visibly correlated. However, there are also certain differences. Ukraine's national bank has imposed a ceiling on the amount of foreign currency sold to individuals (15 thousand hryvnas per day per bank). Besides, a levy of 0.5% is imposed on foreign currency purchases, earmarked for covering the Pension Fund of Ukraine's deficit. The goal of such measures is to bring down the demand for foreign currencies, while at the same time preventing a complete isolation of Ukraine's market from the world market. Obviously, these measures resemble those introduced in Cyprus at the time of the banking system's crisis, or in Russia in 1998; they are probably inevitable in a situation when foreign currency outflow cannot be halted. Russia possesses substantial foreign currency reserves (\$ 481.1bn)⁴, which prevent the realization of such a scenario. However, much will depend on government policy, because over the period from late November 2013 through April 2014, Russia's gold and foreign currency reserves shrank by \$ 40bn, or by nearly 8%.

The IMF's recommendation that the number of military personnel and government officials should be reduced in order to bring down budget expenditures is a

1 The author firmly distinguishes between these licenses and the licenses issued, for example, by self-regulatory organizations in response to newly emerged market demand for professional services in a specific field of economic activity, with due regard for both the ecological safety standards and consumer safety standards established for a particular commodity (or work or service), and for average market price of that commodity, so as to prevent a producer from capturing the market and establishing a single-price monopoly as a sole provider of that commodity (or work or service).

2 N. Petrova, Sushite salo [Start Hoarding Lard]. See kommerisant.ru/doc/2432559

3 Putin prizval ne speshit' s izmeneniyem biudzhethnogo pravila [Putin Spoke against Any Hasty Alterations to the Budgetary Rule]. See ria.ru/economy/20140417/1004331592 or 17 April 2014. 'Considering the risks in the world economy – not only those in our economy, I would still not attempt to alter the budgetary rule in a hurry. But this is a decision in the competence of the RF Government', said Putin to mass media representatives after the broadcast of Direct Line with Vladimir Putin on Channel One in April 2014.

4 See cbr.ru/hd_base/default.aspx?Prtd=mrrf_m

standard requirement at the time of economic decline. Russia has managed to tackle that problem relatively painlessly, by freezing salaries at government budget-funded institutions and allowing these institutions (subordinated to certain ministries – the RF Ministry of Health Care, the RF Ministry of Education and Science, etc.), including the power structures (the RF Ministry of Internal Affairs) to render commercial services to the population, while at the same time separating the budget-funded and off-budget components of their activity. Thus, a collapse of the budgetary system was prevented, and criminal racket as a means of market redistribution was not allowed to flourish (the buildings remained state property in spite of the bad financial situation faced by the management, while the government officials in charge of these institutions could provide, on a paid basis, the government services that were in high demand on the market). This helped to curb the growth of government expenditures, while at the same time satisfying society's demand for government services. As a result, in 2012 Russia succeeded in implementing a very complex large-scale reform of budget-funded institutions by reorganizing them into not-for-profit organizations or joint-stock societies without social upheavals. If Ukraine now simply carries out a one-time massive cut in the number of civil servants and military personnel, it may soon have to deal with grave social problems. And this measure will by no means remove the problem associated with budget deficit, as the newly unemployed and their families will have to be kept at the budget's expense (unemployment benefits, the cost of budget-funded medical care), they will be faced social degradation – a factor preventing their successful adaptation to the market situation.

Another controversial point in the economic transformations in Ukraine is the newly developed scheme for raising taxes. At present, taxes in Ukraine are comparable to those in Russia (value added tax (VAT) at a rate of 20%, tax on profit at a rate of 18%). The levying of VAT on grain and pharmaceutical exports means that the export-oriented industries (the source of foreign currencies) will be deliberately destroyed, because these products will be made exempt from local VAT in the importer epax countries, so the losses incurred by exporters will simply be increased by the amount of additional domestic VAT. The dramatic growth of production costs will diminish the competitive capacity of these commodities on the external market (with their already well-established market prices and profit rates). We believe that VAT must not be levied on exported market products. It is another matter that VAT transferred as advance payments, to be subsequently set off (or refunded) after the sale of foreign currency

received as proceeds (the mechanism that had been applied in Russia prior to the switchover to a system of bank guaranteed granted against advance payments of VAT on exports).

In spite of the announced RF Government's decision not to increase the tax burden until the end of the current political cycle – that is, until 2018¹, it can be assumed that the *tax burden* in this connection was not understood to include the so-called 'inflation' tax, when fluctuations in the ruble's exchange rate result in a redistribution of financial resources across society: the government obtains some additional ruble-denominated resources, while individual ruble-denominated savings and current salaries are depleted of their former value. That is why the emergence of an additional sum of approximately Rb 1 trillion is regarded by RF authorities not as an addition to the existing tax burden, but as a supplementary source of internal funding for the government (these additional funds, as stated by the RF Ministry of Economic Development, instead of covering running budget expenditures will replenish the National Welfare Fund (NWF)²). However, RF authorities should be cautioned against any further attempts to generate such 'additional resources denominated in rubles', resulting from a speculative decline of the Russian national currency's exchange rate.

Any *quantitative easing* policy³ is always fraught with increased risks. But whilst the concentration of financial resources in the US market results in price fluctuations in that country's financial markets (an equivalent of rising financial risks), the upshot of quantitative easing in other economies will be somewhat different. Capital that is not ready to accept the excessive speculative financial risks on US markets will inevitably flow back into those developing markets where investment in real assets will produce a yield comparable to the return on investment in the developed economies, but cleared of financial risks. If Russia's national currency's exchange rate will continue to plummet at an accelerated rate, a cheap US dollar will, most likely, cause further weakening of the ruble, or it will be altogether ousted – in other words, the result would be a hidden 'dollarization' of all settlements in domestic economic

1 'Shuvalov: the tax burden will not be increased in the nearest future. The document "Main Directions of Tax Policy until 2017" will be extended to the end of the current political cycle – until 2018'. See itar-tass.com/ekonomika/1105431, 8 April 2014.

2 P. Mileshkin, Ulyukaev predskazal ekonomike svetloe budushchee. Oslableniie rublia pomozhet popolnit' federal'nyi biudzheta na 900 milliardov [Ulyukaev Predicts a Bright Future for the Economy. The Ruble's Weakening Will Help to Replenish the Federal Budget by Rb 900bn]. See utro.ru/articles/2014/04/16/1189721.shtml

3 This policy is understood by us as a policy aimed at satisfying the economy's demand for financial resources by means of 'liquidity injection'.

transactions, and the ruble will no longer be used as a currency for saving and capital accumulation¹. Russia has already experienced the consequences of a refusal to make settlements in rubles – this was at the turn of last century. This problem cannot be solved by means of prohibitory legislation alone. Russia is still importing the bulk of consumer commodities in demand on her domestic market. In view of a declining ruble, inflationary expectations will, most likely, be on the rise, thus pushing up the level of prices for imported consumer items. Similar problems will also be faced by those investors who take loans denominated in foreign currencies on international markets in order to buy hi-tech equipment and technologies. As a result, investment in the modernization of fixed assets and development of the industrial production base will be shrinking.

At present, it is imperative for Russia to pursue a very moderate labor remuneration policy in the state sphere and the spheres closely linked thereto, abstaining from the allocation of ‘additional ruble-denominated funds’ to social expenditure items and the upkeep of the government. The National Welfare Fund is a government reserve, and so any money spent from it belongs to the category of government expenditure. We believe that, in a situation characterized by shortage of affordable bank loans needed for revival of small and medium-sized businesses, it can be possible to re-channel some of the money earmarked for transfer to the National Welfare Fund, for the financing of commercial investment projects implemented under the joint control of representatives of government agencies, state corporations and the business community. Funding can be channeled through several public non-governmental investment funds by means of short-term (for a period under one year) returnable investment (not to be spent on financial assets, or to be used as a business turnover loan, or to cover commodity purchases, or to cover the costs of raw materials extraction, etc.), the interest on which can be used by the investment funds to strengthen their financial base.

The most important normative documents issued during the period under consideration are as follows:

1. The RF Ministry of Finance’s letter, of 9 April 2014, No 03-00-RZ/16236 offers clarifications with regard to a number of issues concerning the existing double taxation avoidance agreements (hereinafter to be referred to as Agreements) in the part of benefit application terms and tax agents’ liabilities towards the RF budget. This letter should be considered within

the context of anti-offshore measures being taken by the RF government.

The Ministry of Finance points out that for an entity to be recognized the actual (beneficial) owner of the income, the relevant entity should not only be legally entitled to receive the income, but it should also be an immediate beneficiary, i.e., be entitled to decide economically how and when to dispose of the income. Thus, the mere formal fact of ‘tax residency’ should not be deemed to be sufficient for an entity to be granted a tax benefit. The case in point is some intermediate entities situated in the countries which have signed bi-lateral double taxation avoidance agreements with Russia, but actually transfer the income received by Russian taxpayers to entities that are residents in some other state, which has not signed a bi-lateral double taxation avoidance agreement with Russia. The RF Ministry of Finance explains that an intermediate entity, for example a conduit company², should not be deemed to be an entity entitled to actual ownership of the received income and to the corresponding tax benefits if such a company, despite its formal status of income owner in a transaction with a person that is tax resident in the state where the source of that income is situated, has very limited authority over the said income, being in fact a trustee or manager acting in the name of other interested parties. The issue of requalification of the subject of an international commercial agreement clearly falls outside the jurisdiction of the tax authorities and poses a very tough task even for the judicial authorities. At the same time, by Ruling of the Plenum of the RF Supreme Arbitration Court, of 30 July 2013, No 57 it has been established that a tax agent should be responsible for correctly calculating the appropriate amount of the tax and for withholding it at the source (including the correctness of application of the tax benefits (reduced rates and exemptions) envisaged by international double taxation avoidance agreements). As a result, all the risks for conduit companies will become apparent and taken into account in advance. However, in the event of systemic non-recognition, by the tax authorities, of such companies’ right to tax benefits, coming hand in hand with hampering of their even most ordinary commercial transactions and coupled with the additional administrative demand that the ownership right, of a foreign resident, to the received income should be properly confirmed,

¹ Situations when a stronger currency pushes out a weaker one have always been the rule rather than the exception in modern financial history.

² A conduit company (from French *conduit* – a pipe) is a holding company formed in order to reduce the amount of tax burden in the course of international transaction by serving as a pipeline for income from one country to another. Conduit companies are usually established in countries (or territories) with softer tax regimes or in countries that have signed bilateral double taxation avoidance agreements.

Russian organizations may easily lose their investors and, as a result, suffer considerable losses.

It should be added that all these observations and conclusions clearly point to the necessity, for Russia, to join the existing international systems of automatic information exchange. However, it is likely that the current economic sanctions can make the settlement of this issue in the nearest future all but impossible. In any case we believe that, in order to avoid a massive exodus of investors from the RF, any sanctions against Russian organizations – tax agents should be imposed only after it has been proved that those tax agents are indeed misusing the tax benefits granted to them under international agreements¹.

2. Federal Law, of 2 April 2014, No 52-FZ has introduced the following alterations to the RF Tax Code (RF TC):

a) Taxpayers – physical persons paying property and transport taxes on the basis of tax notices are now obliged to submit, to the relevant tax body, the aforesaid tax notices and copies of the documents establishing (or certifying) their ownership rights to the relevant immovable property objects and (or) copies of the documents in confirmation of State registration of their motor vehicles. Such documents should be submitted to the relevant tax body in respect of each of the objects of taxation once a year, before 31 December of the year following the expired tax period. The failure (or delay) to submit the aforesaid information should entail tax liability: a fine at a rate of 20% of the unpaid amount of tax;

b) As a result of the recent change in the status of budget-funded institutions, whereby these have been made subject to Russia's legislation on non-commercial organizations, those Federal Treasury's bodies where the client accounts of budget-funded organizations are operated, should be obliged to inform the tax relevant authorities about the opening and closure of client accounts, as well as about any changes in the format of such accounts, exactly as it is done by the credit institutions operating the client accounts of taxpayers;

c) The simplified taxation system, whereby exemptions are envisaged from the profits tax (except for the profits from the dividends and interest on government securities), from the property tax (except for the assets which are taxed at their cadastral value), from VAT

(except for VAT on imports), and a 6% rate of tax is set for income, or a 15% rate for the difference between income and expenses, has now been made available to organizations established by budget-funded and autonomous institutions for the purpose of materializing the results of the intellectual activity of these budget-funded and autonomous institutions in those cases when the exclusive rights to the results of the said intellectual activity are not only held by these (scientific) budget-funded and autonomous institutions in full, but are also held jointly with third parties. The purpose of this decision is to give an impetus to said third parties to increase their cooperation with educational and scientific institutions in business matters and other joint activities, as well as in implementing the results of joint intellectual projects.

3. The RF Ministry of Finance's letter, of 27 January 2014, No 03-11-09/2884 and the Federal Tax Service of Russia's letter, of 7 April 2014, No GD-4-3/6312@ contain a very important clarification concerning the procedure for issuance of licenses to individual entrepreneurs in 2014.

In accordance with the RF TC, the tax for the patent issued to an individual entrepreneur should be calculated at 6% of the potential annual income expected to be received thereby within the framework of one or other business activity. The amounts of potential annual income should be established by the laws of the subjects of the Russian Federation (clause 7 of Article 346.43 of the RF TC) for all types of entrepreneurial activities in relation to which the patent system of taxation can be applied. At the same time, the minimum amount of the potential annual income expected to be received by an individual entrepreneur cannot be less than Rb 100,000, while the maximum amount in the same instance cannot exceed Rb 1m. The minimum and maximum amounts of the potential annual income expected to be received by an individual entrepreneur are eligible for indexation by the deflator coefficient set for the corresponding calendar year (*ibid*, clause 9). By Order of the RF Ministry of Economic Development, of 7 November 2013, No 652, the deflator coefficient for 2014 is set at 1.067.

According to legislation, a relevant tax body is obliged to issue a patent to an individual entrepreneur applying for it within 5 days since receiving the application. Therefore the tax body does not have the right to reject this application on the ground that the law of the corresponding RF subject, whereby the amounts of potential annual income expected to be received by individual entrepreneurs in the next calendar year is to be set, has not yet been adopted. Should this indeed be the case, then the cost of the patent is to be deter-

¹ As follows from the clarifications provided by the Constitutional Court of the Russian Federation (RF CC), international agreements should be deemed to be an element of Russian Federation's domestic legislation, and therefore must be observed by all government institutions on a regular basis, and not only in response to a court ruling.

mined on the basis of the 'old' initial data, to which the 2014 deflator-coefficient should be applied.

As far as the status of individual entrepreneurs is concerned, the clarifications provided by Russia's Ministry of Finance and the Federal Tax Service (FTS) have, in fact, totally eliminated the danger of administrative procrastination that may result from delays in the passage, by one or other RF subject, of the relevant laws. In the event when the maximum and minimum amounts of potential annual income for some types of entrepreneurial activities, established by the relevant RF subject's law for 2014, are increased (or decreased) in comparison with those being rested on by the tax body when issuing the patent, the tax body should issue to the taxpayer a new patent with the updated tax amount.

4. It should be noted that the RF Ministry of Finance continues its fruitful activity aimed at removing all the other administrative obstacles that are economically counterproductive for taxpayers. Thus, in the RF Ministry of Finance's letter, of 10 April 2014, No 03-03-RZ/16288 it is noted that any primary documents attesting to the validity and nature of production costs, including the costs of hospitality, may serve as confirmation of the fact of such costs having been incurred for profits tax purposes, including tax deduction. In particular, the document confirming the validity of hospitality may be a summary report on expense accounts, approved by the head of the organization and confirmed by relevant primary documents.

5. The RF FTS's letter, of 7 April 2014, No GD-4-3/6391@ clarifies the issue concerning the procedure for paying Mineral Resource Extraction Tax (MRET).

In accordance with the RF TC, a MRET payer carrying out mineral extraction at several sites situated in the territory of one subject of the Russian Federation, has the right to be registered with the tax authorities of the territorial administrative unit where one of the above sites is situated. As far as the filling up of a tax declaration is concerned, this means that the taxpayer should now enter, in sub-section 20 of the Declaration's Section 'The Amount of Tax Payable to the Budget', the OKATO code of the municipal formation where the said taxpayer is registered as a MRET payer. Bearing in mind that the RF Tax Code stipulates that 'the tract of sub-soil granted to the taxpayer for use shall be recognized to be the territory of the subject of the Russian Federation where the tract of sub-soil is situated' (clause 1, Article 335 of the RF TC), the OKATO code of the tax body selected by the payer of MRET will by no means principally affect the identification of the actual recipient of this income.

The procedure for entering MRET revenues into various budgets is regulated by the budgetary legislation of the Russian Federation. The distribution of MRET revenues among the budgets of Russia's budget system is carried out on the basis of the aggregate amount of tax receipts under the relevant code of the RF budget classification.

6. The RF FTS's letter, of 15 April 2014, No GD-4-3/7123@ states that the free of charge transfer of ownership rights to excisable goods from one person to another, carried out for promotional purposes, should be deemed to be the sale of goods, and thus subject to excise duty. We believe that the tax authorities should have been provided with a more precise clarification in order to avoid any possible distortions of existing legislation in the future. Promotional campaigns are designed to promote goods (or work, or services), and in this capacity they represent a form of advertizing. Therefore they should be entitled to the same benefits that are established for advertizing goods (or work, or services). In particular, in accordance with the existing procedure for the transfer of excisable goods (or work, or services) carried out for promotional purposes in the territory of the Russian Federation, the transfer, for advertizing purposes, of goods (or work or services) should be made exempt from VAT, provided that the cost of acquiring (or creating) a unit of those goods (or work, or services) does not exceed 100 rubles (sub-clause 25, clause 3, Article 149 of the RF TC). At the same time, in accordance with clause 16 of Article 270 of the RF TC, expenses in the form of the value of assets (or work, or services), which are transferred free of charge, and expenses associated with such transfer, should not be taken into account when determining the tax base, and therefore should not be deemed to be tax-deductible.

7. Joint letter of the RF Ministry of Finance and the RF FTS, of 4 April 2014, No GD-4-3/6132 specifies the situations where persons who are not payers of VAT should also be made exempt from the obligation to submit VAT declarations. According to the letter, this exemption should be extended to: 1) those organizations and individual entrepreneurs whose entire amount of income received from the sale of goods (or work, or services) generated over the course of three previous successive calendar months does not exceed Rb 2m before VAT; 2) the taxpayers using the simplified system of taxation (except for VAT on imports); 3) the payers of a single presumptive income tax – within the framework of their entrepreneurial activities subject to this tax (except for VAT on imports); 4) the payers of a single agricultural tax (except for VAT on imports);

and 5) entrepreneurs who have switched over to the patent taxation system.

8. Joint letter of the RF Ministry of Finance and the RF FTS, of 24 March 2014, No BS-4-11/5295 communicates to the tax authorities the procedure for reconciling information on immovable property entered into the Unified State Register of Immovable Property and Transactions Therewith (EGPR) with information contained in the databases of regional authorities of the Federal Tax Service. The purpose of the said procedure is to make it possible for the tax authorities to timely compose and issue tax notices to taxpayers, specifying

the amount of their immovable property tax. In order to coordinate the activities of the RF FTS and the EGPR, these federal institutions have established a special interdepartmental task force. The RF FTS was to submit the initial list of immovable property objects to the EGPR before 28 March 2014. The time limit for the EGPR to consider the said list was set at 30 days. For our part, we believe that such interdepartmental task forces should operate on a permanent basis, because otherwise it would be technically difficult to update on a timely basis the lists of real property objects contained in the databases of regional authorities of the Federal Tax Service. ●