AN OVERVIEW OF NORMATIVE DOCUMENTS ON TAXATION ISSUES FOR JULY–AUGUST 2014

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In the period under consideration, as a result of restrictions imposed by Russia on food imports from those countries that had introduced sanctions against the Russian Federation or those that have joined the anti-Russian economic policy, the domestic market was being artificially limited. This inevitably pushed up food prices. Now the 'people's deputies' are putting forth proposals to the effect of imposing legislative constraints on product profitability and price level. If such a law is actually passed, it can be expected that certain types of goods will be in deficit, because in a situation of absence of an 'iron curtain' coupled with the ruble's depreciation against foreign currencies Russian products will be exported to those markets where they can be sold at reasonable market prices; as a consequence, the Russian market will have to make do with goods unsellable in other markets. Thus, if we choose to rely on direct administrative methods – that is, follow the deputies' suggestion and introduce price regulation – the situation can only become worse, so that soon products will have to be rationed, and the population will once again have to stand in long lines just to get food and other 'bare necessities'. We believe this to be a dead end – and even more so because of the existence in the RF of taxes on turnover (VAT) and taxes calculated as percentage of earnings (insurance contributions to state off-budget funds), whereby the size of federal budget revenue (or off-budget funds) is automatically linked to the rate of price growth. Evidently, two economic priorities are currently on the agenda: one is to ensure long-term sustainability with regard to the government's social liabilities to the population (primarily the payment of pensions and social benefits); and the other is to avoid raising the tax load on producers and increasing government foreign debt and the foreign debt of state corporations (including the payment of interest on loans).

Recent sanctions have narrowed the opportunities for attracting financial resources from world markets to the RF economy, thus putting to the fore the problem of finding adequate sources of funding to cover the expenditures mapped in the presidential edicts issued in May 2012. In search of such sources, the RF Government resorted to the introduction of sales tax[1] (which had already been introduced and abolished more than once in this country). In our previous review we already pointed out that this tax would be contrary to existing constitutional norms if applied to taxpayers who are subject to special tax regimes. Now it has been suggested that the sales tax at a rate of 3% should be imposed only on trade centers, and the actual right to introduce the tax should be delegated to the level of regions. By way of doing so, the RF Government intends to provide regions with a new source of budget revenue and thus somewhat relieve the currently tricky financial situation faced by regional authorities. It should be noted that it will be technically difficult to actually levy sales tax on certain selective taxpayer categories (it will be necessary to elaborate criteria for selecting appropriate taxpayers, determine the types of goods, work and services to be made exempt from the tax). If this task is successfully accomplished, the introduction of sales tax will probably bring down the level of the population's real income. Given the prospects of the price/wage spiral being triggered in conjunction with the prices rising on the domestic market in response to disappearance of imports, the one-time negative impact of the introduction of sales tax on real consumption may become somewhat leveled down. After several years of an accelerated growth rate displayed by wages vs. labor productivity's growth rate, the constraints on physical volumes of consumption imposed by rising prices may boost competition between domestic producers, because imported goods in any event will be sold at prices no lower than those set on the world market (estimated in foreign currency terms), while domestic products are estimated in rubles.

The decisions concerning placement of the resources held by the National Welfare Fund (NWF) on accounts with state financial monopolies (state corporations, banks with state participation) appear to be quite controversial in nature.

Thus, by Order of the RF Government of 2 August 2014, No 1451-r the Memorandum on Financial Policy issued by State Corporation 'Bank for Development and Foreign Economic Affairs (*Vneshekonombank*)' (VEB) has been augmented by new provisions where-

1 V boi idut nalogi. Vybor mezhdu liberalizatsiei i mobilizatsiei rossiiskoi ekonomiki, kazhetsia, sdelan [Taxes Come to the Battlefield. It Seems That the Choice between Liberalization and Mobilization Has Been Made]. See www.gazeta.ru/comments/2014/08/01_e_6154157.shtml

by the sources of *Vneshekonombank*'s equity (which are taken into account when estimating its debt ceiling) may include deposits answering the following requirements: they cannot be withdrawn before term; their term cannot be less than 5 years; a deposit is to be redeemed as a last priority, after claims presented by all other creditors have been satisfied. So, the Order determines the conditions on which the monies of the National Welfare Fund attracted by a bank in the form of a deposit may be treated, for technical purposes, as that bank's equity.

At the same time, the alterations to the requirements to financial assets in which the resources of the National Welfare Fund may be invested, which have been introduced by Decree of the RF Government of 31 July 2014, No 739, stipulate mandatory terms to be incorporated into the text of a deposit agreement concluded by the National Welfare Fund, and these terms give rise to some questions. Thus, for example, the RF Government directly prescribes (or orders it to be mandatory) that the text of a deposit agreement should incorporate provisions whereby a bank and its management, in an event of losing the monies placed with that bank by the National Welfare Fund, are to be relieved of all responsibility relating to such a loss.

For instance, 'Item 12 of the requirements … shall be augmented by Subitem "c(1)" of the following content … the NWF's resources may be placed as deposits denominated in US dollars … on condition of compliance with the following terms … a deposit agreement shall contain a provision that, in an event of liquidation of State Corporation 'Bank for Development and Foreign Economic Affairs (*Vneshekonombank*)', the claims pertaining to such a deposit shall be satisfied after the claims of all the other creditors have been satisfied [1]; … a deposit agreement shall stipulate a condition that, if the base capital sufficiency norm shrinks to a level below 2 percent, the unpaid interest on the deposit shall not be redeemed and shall not be accumulated due to termination, in full or in part, of the obligation of State Corporation 'Bank for Development and Foreign Economic Affairs (*Vneshekonombank*)' to pay the accumulated amount of interest on the deposit, in this connection the obligation of State Corporation 'Bank for Development and Foreign Economic Affairs (*Vneshekonombank*)' to repay the sum of main debt against the deposit shall be terminated in full or in part (in an event of losses incurred by State Corporation 'Bank for Development and Foreign Economic Affairs (*Vneshekonombank*)', with the result of shrinkage of the base capital sufficiency norm to a level below 2 percent, on condition that the undistributed profit and reserves have been used to cover the losses of State Corporation 'Bank for Development and Foreign Economic Affairs (*Vneshekonombank*)'. In accordance with the alterations approved by the RF Government's Decree, it is formally forbidden for representatives of the State to conclude an agreement concerning the placement of the NWF's resources as a deposit on conditions other than those stipulated here. Since the ways that the National Welfare Fund's resources may be invested are regulated primarily be prevailing legislation, we believe that the text of an agreement concerning placement of the National Welfare Fund's resources as a deposit with *Vneshekonombank* should likewise strictly conform to the legislative acts regulating the directions for using these funds and the purposes thereof.

The differences in standpoints between government financial departments and the Russian Union of Industrialists and Entrepreneurs (RSPP) with regard to the 'de-offshorization' issue have not been properly settled by the existing regulations[2]. This has to do with the introduction, into the RF Tax Code (RF TC), of rules for levying taxes on profits of controlled foreign companies (CFC), as well as the criteria for recognizing a foreign legal entity to be a controlled foreign company. The RF Ministry of Finance suggests that this should be done by a complete survey method. The Russian Union of Industrialists and Entrepreneurs, for its part, suggests that that the rate of tax levied on profits of affiliations of Russian legal entities, which are situated in countries with easy taxation regimes that have signed double taxation avoidance agreements with the Russian Federation (Cyprus, Switzerland, etc.), with the exception of affiliations of companies belonging to the fuel and energy complex and banks), should be increased to 9%. It is proposed that the scheme for supervising controlled foreign companies elaborated by the RF Ministry of Finance should be applied only to genuine offshore companies, while at the same time providing them with adequate conditions for painless reinvestment, in Russia, of their capital held in those offshore zones. In particular, it is suggested that investment in securities issued by Russian companies in an amount no less than 25% of the investor's capital should be made exempt from profits tax – 'that is, to make exempt from taxes the repatriation of profit generated in offshore zones, if it is directly invested in fixed assets in the Russian Federation"[3].

1 The RF Government 'prescribes' – that is, makes it mandatory to conclude a deposit agreement only on such terms.

2 D. Butrin, Zaofshorennyi vzgliad. RSPP gotov otkupit'sia ot polnogo nalogooblozheniia svoikh inostrannykh kompanii. [An Offshore Look. The RSPP (Russian Union of Industrialists and Entrepreneurs) is prepared to pay for making its foreign companies exempt from full taxation]. See kommersant.ru/doc/2542801 of 11 August 2014.

3 Ibid.

These proposals, in our opinion, deserve to be thoroughly considered, because they address the issue of direct investment in capital of Russian legal entities. Any other ways of attracting investment into the Russian economy are at present very limited.

The normative documents issued over the period under consideration (while the lawmakers were on their summer vacation) dealt in the main with technical issues.

1. By Letter of the RF Ministry of Finance of 9 July 2014, No 03-06-05-01/33375 and Letter of the Federal Tax Service of Russia (FTS of Russia) of 14 August 2014, No AS-4-3/16135, taxpayers and tax agencies are informed of the fact that the Rules for keeping records on natural gas approved by Order of the RF Ministry of Energy of 30 December 2013, No 961 are not compatible with the norms stipulated in existing tax legislation, and so they cannot be applied when calculating the amount and effectuating the payment of Mineral Resource Extraction Tax (MRET). The RF Ministry of Finance noted that in the aforesaid Rules it is envisaged that the volume of extracted natural gas should be determined by adding up the quantities of natural gas pertaining to each specific operation, namely: natural gas measured and transferred for transportation; natural gas measured and transferred to unrelated parties; natural gas measured and used to satisfy the producer's own production and technical needs, with due regard for the actual losses of natural gas in the process of its extraction. At the same time, in accordance with the RF Tax Code, the quantity of extracted mineral resource should be determined by means of direct counting method (by applying measuring devices and equipment) or by indirect method (on the basis of estimated values concerning the content of a given mineral resource in the extracted raw material (or waste, or losses).

Thus, Mineral Resource Extraction Tax should be levied on the amount of extracted natural gas, and not on the amount of transported or used natural gas.

2. Letter of the RF Ministry of Finance and the Federal Tax Service of Russia (FTS of Russia) of 12 August 2014, No GD-4-3/15833@ offers detailed explanations of the issue as to who and in which cases should be considered to be a tax agent in relation to dividends paid by a Russian issuer. The Letter also describes the procedure for filling in a tax declaration for profits tax in case of equity participation in other legal entities. The explanations are backed by some numerical examples.

3. By Letter of the RF Ministry of Finance of 21 July 2014, No 03-04-07/35645 and Letter of the Federal Tax Service of Russia (FTS of Russia) of 12 August 2014, No GD-4-3/15825@, explanations are offered as to the issue of levying tax on funds received in the form of a grant to set up a peasant (or farmer) household.

In accordance with provisions stipulated in Article 217 of the RF Tax Code, the money received from the RF budgetary system as grants to peasants or farmers for setting up and developing their peasant (or farmer) households, as one-time payments to start-up farmers for setting up their households, and as payments for developing family farms for livestock breeding are exempt from Personal Income Tax (PIT).

Those farmers who pay the single agricultural tax or apply the simplified taxation system are excluded from this exemption. This happens because PIT is levied on the amount of income from entrepreneurial activity less the expenditures listed as costs to be taken into account when calculating the tax base for profits tax.

The single agricultural tax and the simplified taxation, record-keeping and reporting system (STRR [USNO]) fall into the category of special tax regimes, and so the cost deduction procedure applied in the framework of profit taxation is not applicable to these two regimes. Instead, other schemes for dealing with grants are applied. Thus, under the simplified taxation, record-keeping and reporting system, the amount of income received in the form of subsidy is deducted in proportion to the amount of actual relevant expenditures. Funding from the federal budget in the form of grants for setting up and developing peasant (or farmer) households is allocated only if there exist regional programs for supporting start-up farmers.

4. By Letter of the RF Ministry of Finance of 16 July 2014, No 03-05-04-02/34879 and Letter of the Federal Tax Service of Russia (FTS of Russia) of 30 July 2014, No BS-4-11/14944, the procedure for land tax payment is explained. When levying this tax, its rate should be set depending on the way a given land plot is actually used, and not on its intended use. In particular, the rate of tax to be levied on land plots of agricultural designation is 0.3% of their value, but if no agricultural production takes place in that land plot (the plot is recognized by an empowered body not to be used for agricultural production), the tax on the plot should be levied at the rate set by the representative body of a given municipal formation for other categories of land and no higher than 1.5%, beginning from the tax period during which the decision concerning the identification of the law violation is made and until the beginning of the tax period during which the violation has been corrected.

The exhaustive list of indicia of a land plot which is not being used for purposes of agricultural produc-

tion is approved by Decree of the RF Government of 23 April 2012, No 369.

5. By Letter of the RF Pension Fund (RF PF) No NP-30-26/9660 and Letter of the RF Social Insurance Fund (RF SIF) No 17-03-10/08-2786R of 29 July 2014, in order to ensure uniform application of the norms on insurance contributions stipulated in legislation of the Russian Federation, an overview of answers to questions frequently asked by taxpayers was published, having been prepared in coordination with the RF Ministry of Labor. We believe that in case of recognition, by judicial bodies, of some of the answers offered by state off-budget funds to be incompatible with the norms stipulated in legislation, as well as when the explanations offered by federal ministries are recognized to be incompatible with prevailing legislation, these should, in their turn, be recognized as null and void from the date of their publication.

In this overview it is explained, in particular, that the base for calculating the amount of insurance contributions from the year 2012 has included all the payments made by a given employer to its employee in accordance with the relevant collective labor agreement (material aid, one-time payments to retiring workers, compensation of holiday package cost, targeted social aid, compensation of the cost of medical treatment and medications, the payment in an amount of one average salary to employees – blood donors, payment for the period of being involved in military reservists call-up or a call-up for military reservist training); this rule applies to all payments in money form or in kind made on the basis of provisions stipulated in collective labor agreements or in absence of provisions on some or other types of payments in collective labor agreements (but in the framework of actual labor relations between employers and employees).

In the opinion of the off-budget funds, the payments in compensation of the cost of services of VIP lounges at railway and bus stations, sea and river ports, or airports, made to some employee categories, should not be treated as part of a mandatory business trip cost package (that is, such payments do not represent a form of compensation established by legislation), and so these payments should be included in the base for calculating the amount of insurance contributions.