

## A REVIEW OF TAXATION REGULATORY DOCUMENTS ADOPTED IN THE PERIOD OF NOVEMBER–DECEMBER 2014

L.Anisimova

*It by all means is nearly twofold devaluation of the national currency amid falling crude oil prices that was the key event in the period under review, which determined Russia's economic development vector.*

In the past month, Russia's government more than once provided explanations of its plans on economic, financial and taxation policy. These explanations refer to a period until the 17<sup>th</sup> of December. The Russian President's stance set out in the Presidential Address to the Federal Assembly (the 4<sup>th</sup> of December) includes a few essential points.

The key assignments to the Federal Assembly are to cut federal budget spending in 2015–2017 annually by at least 5% (except defense and national security spending); make sure that operating costs are reduced by 2–3% annually at state-run corporations in which Russia holds more than 50% interest; widen the possibility for small and medium-sized businesses to enter into public procurement contracts; impose a ban, effective since 1.01.2016, on conducting scheduled control and supervision inspections at small businesses; make sure that the terms, established prior to 1.01.2015, of taxation and payment of contributions to The Pension Fund of Russia (RPF), the Social Insurance Fund (SIF), the Compulsory Medical Insurance Fund (CMIF) remain intact between 2015 and 2018; make amendments to legislation of the Russian Federation, stipulating that Russian individuals be relieved of tax and criminal responsibility on a nonrecurring basis under a condition that they will bring back to the Russian jurisdiction the incomes they had gained in the Russian Federation and later transferred, without paying taxes, to foreign jurisdictions; adjust forecasts of Russia's socio-economic development on the basis of a scenario providing for a decline in inflation to 4%, increase of labor productivity by 5% annually while maintaining macroeconomic balance; strengthen the capital of systemically important banks under a condition that they will allocate the received funds to finance at affordable interest rates projects in the real sector of economy, which also includes the use of project financing arrangements, etc.

One cannot but note certain dissonance between the set forth program and the steps that have been taken.

In his Presidential Address Mr Putin noted that tax burden wouldn't increase for the next four years<sup>1</sup>.

1 [lenta.ru/articles/2014/12/04/tezisy](http://lenta.ru/articles/2014/12/04/tezisy) 4 декабря 2014 Декабрьские тезисы. Выступление Президента РФ в Федеральном

Regretfully, this implies neither abolishment nor suspension of the coming-into-force of the tax novations which were adopted prior to 1.01.2015. This refers to the introduction of a sales tax, property tax based on the market value, increase in the assessment base of contributions to the RPF, the SIF, the Federal Compulsory Medical Insurance Fund (FCMIF). These payments together with drastically increased Central Bank's interest rate in 2015 will further constrain the financial potential of manufacturers, and instead of achieving the desired wider scope of budgets' revenues we may eventually see a business downturn, and hence the budget system revenues would be reduced.

The proposal to announce a non-recurrent tax amnesty is controversial too. The introduction of tax amnesty irrespective of types of violations across the country would instantly turn Russia into a huge offshore zone for criminal capital from around the world, even if such an amnesty is non-recurrent<sup>2</sup>. The monetary authorities of other states would instantly take countermeasures aimed at protecting their economies from criminal capital. Should money transfers to the Russian Federation and investment therefrom be subject to anti-offshore policies, this would harm enterprises opened in Russia and operating in good faith, while the rest of investors might simply fold their operations. We believe that capital should be administered prudently rather than by wholesale. Additionally, an apparent contradiction arises in the state policy: on the one hand, the Investigative Committee of Russia has just recently been re-empowered to launch criminal cases for non-payment or late payment of taxes even in case of paid off tax violations. On the other hand, a large-scale amnesty of capital would cover the capital which, among other things, might have been accumulated as a result of tax evasion, embezzlement, or through criminal operations. Furthermore, if capital is legalized on the territory of other states, then Russia

собрании [December 4, 2014 December Theses. Presidential Address to the Federal Assembly]

2 [lenta.ru/articles/2014/12/04/tezisy](http://lenta.ru/articles/2014/12/04/tezisy) 4 декабря 2014 Декабрьские тезисы. Выступление Президента РФ в Федеральном собрании или См. там же. [December 4, 2014 December Theses. Presidential Address to the Federal Assembly or see *ibid*]

is no longer regarded as the place of origin of such capital. Capital which was pulled and legalized in other states cannot be expected to return in big volumes unless investment provide returns high enough to cover the risks of investment on the territory of the Russian Federation.

The issue of strengthening banks' capital under the circumstances should be addressed with caution. For instance, a law stipulating the transfer of Rb 1 trillion to strengthen the capital of largest (presumably state-run) banks has been adopted, whereas the State Duma is planning to monitor on a constant basis that the money goes to manufacturers financing major investment projects. In fact, a system of centrally-planned-economy relations seems to be restored: financially ailing banks are going to be integrated into the public distribution scheme as transmission mechanisms designed to formally provide loans to loss making manufacturers so that the latter can keep manufacturing/producing unmarketable goods (works, services) to be subsequently purchased by the state under the veil of government contract execution and paid with reducing revenues from sales of mineral resources in a free market.

To maintain a sustainable banking system, the insured amount of retail deposits is planned to increase to Rb 1,4m from Rb 700,000. The endeavor is noble indeed. As a reminder, it is banks' money that is paid as contributions to the deposit insurance fund. Doubling the retail deposit insurance liabilities, the Central Bank of Russia is lifting the crucial limits on using the liquidity which banks borrow from other depositors: obligatory reserve amounts get smaller, capital adequacy requirements are revised, i.e. it would be as cheap as possible for banks to borrow in the market. As a result, the Central Bank of Russia basically reduces the system which protects manufacturers' financial resources attracted as deposits. Therefore, the decisions to be made produce a two-fold result.

The economic community points to the need for developing an explicit road map of measures for the Russian Government and the Central Bank of Russia to deal with the current situation<sup>1</sup>.

Another marked initiative was launched late in 2014. Based on the information published in the economic press, the Finance Ministry of Russia may bring back GKO, short-term ruble-denominated treasury bills, to the market. For most of the Russians the bills are best remembered for the default that occurred in 1998<sup>2</sup>.

1 Е. Гонтмахер, Как рассосется? Сайт МК.ru от 21.12.2014 г. [E. Gontmacher, How does it go away? МК.ru 21.12.2014]

2 Л. Царева, Д. Ладыгин, Россия избавилась от комплекса ГКО. Минфин возвращается к коротким рублевым займам. Сайт [kommersant.ru/doc/2618347](http://kommersant.ru/doc/2618347). «Уже в следующем году Минфин

The purpose of these bills still remains to be clarified. The Head of the Treasury explained that there is a plan to provide budget resources against GKO overnight for a fee, i.e. make it possible for buyers to cover short-term cash deficiency using REPO schemes and for the federal budget to generate revenues.

The question of principle is whether or not the tax allowance will be restored for difference between the purchase price and the sale price of GKO. It is this difference that was stated as income from GKO and exempted from taxation. The tax exempted difference between the purchase price and the sale price turned GKO into "a money printer". If GKO see a strong demand, neither the Finance Ministry of Russia, nor the Treasury, nor the Government of Russia would be able to restrain themselves from increasing GKO in volume, because strong demand implies the opportunity to generate extra income. It is quite easy to artificially create "a money printer" – losses should be separated from gains. Losses from the difference in GKO price are "accrued" to a person who provides a loan to purchase GKO (no tax base will eventually arise for this person: losses from default on the loan are written off via going down profits from other types of operations which are put to reserve, e.g. foreign exchange gain<sup>3</sup>), while tax-free and risk-free income arises for the person who presents GKO for redemption. Furthermore, the purchase and sale transactions may be unlimited in number. Those who initiates GKO have forgotten that the damage from GKO is not just the amount paid during the redemption over that paid during selling. A combination of GKO and tax allowance can produce endless "losses" whereby creating an opportunity to avoid taxation on other types of income generated in the national economy. This is especially dangerous in times of highly volatile exchange rate. It stands to reason that the Tax Code of Russia defined that the interest on securities is previously stated (established) income – and only such income may be exempted from taxation. The difference between the purchase price and the sale price of GKO, if such bills are introduced, must be taxable at a rate exceeding the rate of the tax on interest on securities.

может начать размещать государственные краткосрочные облигации (ГКО). Об этом вчера на заседании бюджетного комитета в Совете Федерации заявила первый заместитель главы Минфина Татьяна Нестеренко.» [L. Tsaryova, D. Ladygin, Russia has recovered from the GKO complex. The MinFin is back to short-term ruble-denominated loans. [kommersant.ru/doc/2618347](http://kommersant.ru/doc/2618347). "The MinFin may begin as early as next year to place short-term ruble-denominated treasury bills (GKO). First Deputy Head of Finance Ministry Tatyana Nesterenko said about this yesterday at a meeting of the Federation Council Budget Committee."] 3 GKO tend to gain popularity in times of highly volatile exchange rate.

A series of taxation regulatory documents were adopted in the period under review. The following of them are of most interest:

1. The Federal Law of 29 November 2014 No. 382-FZ made amendments to the Tax Code of Russia.

The foregoing Law introduced as compulsory payment a tax on the right to run certain types of business operations within a given territory. Municipalities as well as the cities of federal importance were empowered to collect the tax.

The same Law introduced a sales tax as local tax (Chapter 33 of the Tax Code of Russia). The sales tax to be paid to municipal budgets and the budgets of cities of federal importance may be introduced directly by municipal administrative bodies, legislative bodies of the cities of federal importance. Additionally, they may determine tax allowances and terms of spending of the tax revenue. Individual entrepreneurs covered by the patent system of taxation, and taxpayers covered by the system of taxation of agricultural producers (unified agricultural tax) are exempted from this tax. The use of a movable or immovable property item in the course of business at least once per quarter is recognized as taxable item. The retail tax rate may not be less than the value of a patent as per 50 square meters of the occupied surface. The tax rate on the retail market organization activity may not exceed Rb 550 per square meter of a retail market surface. The foregoing tax rate is subject to annual indexation using the deflator coefficient. The taxpayer shall self-assess and pay the tax not later than on the 25th date of the month following the reporting period (quarter). This tax may be accrued to the costs when the profit tax is paid. The sales tax is to be introduced on or after 1.07.2015.

The foregoing Law updated to the procedure of payment of the value added tax (VAT) – from now on, services provided by air carriers whose points of departure and destination are located outside the Russian Federation are deemed to be services rendered on the territory of Russia if an aircraft has a stop on the Russian territory and the place of arrival of goods is the same as the place of departure thereof from the territory of Russia. This regulation is subject to a 0% rate, however, the documents envisioned for cases of transit carriage, i.e. bearing notes made by customs authorities, must be provided to tax authorities in order to substantiate the eligibility to the preferential rate.

The procedure for payment of the personal income tax (PIT) was updated. In particular, a provision is made for tax allowances when immovable property items are sold. An aggregate 5-year period of owning a property has been introduced for the entitlement to tax exemption when selling such property. However, if a property

is purchased by way of inheritance or any other situations provided for by the Tax Code of Russia, then the period is to be reduced to three years. An allowance is made for using a decreasing coefficient to taxable income if a revenue from selling the property appears to be less than the cadastral value thereof.

A list of deductible contributions to be paid under voluntary types of insurance was extended: in particular, this preference is granted under voluntary life insurance for a period of more than five years, which was concluded for one's own benefit or for the benefit of immediate family members (next of kin).

2. The Federal Law of 29.11.2014 No. 380-FZ made amendments to the Tax Code of Russia, which regulate the application of tax preferences due to the adoption of Federal Law on Advanced Economic Development Zones (AEDZs), including VAT refund and the application of the institution of suretyship for the purpose of VAT payment liability; application of a 0% rate of the profit tax paid to the federal budget; application of a reduced rate on the profit tax charged to regional budgets (not more than 5% within the first five tax periods and 10% within subsequent tax periods); application of preferences<sup>1</sup> relating to the mineral extraction tax. To be entitled to tax preferences, a Russian organization may not be resident of a special economic zone (SEZ), may not be subject to special tax treatments, may not participate in a consolidated group of taxpayers, be resident of other AEDZs or participate in regional investment projects, and it may not have stand-alone units outside AEGZ.

3. The Russian Government Executive Order of 04.12.2014 No. 1316 increased, effective from 1.01.2015, maximum amount of the base for the assessment of insurance contributions from the RPF and the SIF. The maximum amount of the base for contributions to the SIF and the RPF will be Rb 670,000 and Rb 711,000 respectively.

4. The Letter of the Federal Tax Service of Russia (FTS of Russia) of 08.12.2014 No. GD-4-3/25307@ clarified the period of including accounts payable with expired statute of limitations into the profit tax base, which are subject to accounting for tax purposes as of the date of expiration of the statute of limitations (Paragraph 4 Article 271 of the Tax Code of Russia).

5. The Executive Order of the FTS of Russia of 26.11.2014 No. MMB-7-11/598@ approved the blanks and the format of notifying a tax authority of the existing immovable property items and/or means

<sup>1</sup> Coefficient, which provides characteristics of the production site and is used in the mineral extraction tax calculation formula, is taken to be equal to 0 within the first 24 tax periods; then it increases by 0.2 upon expiration of each of the 24 subsequent tax periods, up to and including 120 tax periods.

of transport which are recognized as taxable items. Effective January 1, 2015, natural persons who receive no tax notices and pay no property taxes on the real estate items and means of transport which they own are obliged to notify tax authorities of such property items in electronic format via telecommunications channels.

6. The Letter of the FTS of Russia of 08.12.2014 No. GD-4-3/25301@ describes the letter of the Finance Ministry of Russia of 19.11.2014 No. 03-06-05-01/58794 on the criteria of applying the decreasing coefficient for the mineral extraction tax with regard to regional gas supply systems. A gas supply system is recognized as regional, provided that the system is not integrated into the Unified Gas Supply System, is operating basically within a give region and controlled by authorized regional government bodies.

7. The Letter of the FTS of Russia of 02.12.2014 No. GD-4-3/24869@ concerning taxation of the income of foreign organizations as penalties for violation of contract terms clarifies that the incomes mentioned in double taxation conventions are subject to taxation only in the resident's state which is the contracting state. Thus, penalties imposed for the violation of contract terms are subject to taxation at

the place of fiscal residence of the recipient of such penalties.

8. One cannot but note that the Russian Federation keeps adopting and refining technical documents regulating the generally accepted rules for accounting of income and expenses of manufacturers amid free market relations. For instance, the Finance Ministry of Russia's Executive Order of 30.10.2014 No. 127n introduced on the territory of Russia the International Financial Reporting Standards (IFRS) "Accounting of acquisitions of interests in joint operations (Amendments to the International Financial Reporting Standard (IFRS) 11)" and "Clarification of acceptable methods of depreciation (Amendments to the International Accounting Standard (IAS) 16 and the International Accounting Standard (IAS) 38)". Both documents regulate the procedure for accounting of income and or deduction of expenses based on the fair market value of an asset as of the date of operation.

The foregoing letter clarifies that organizations must apply the amendments to the IFRS with regard to transactions (expenses) which are conducted in the period when the amendments are introduced and in subsequent periods, whereas the amounts recognized in the previous periods must not be adjusted. ●