

TAX HOLIDAYS FOR INDIVIDUAL ENTREPRENEURS: MODERN CONCEPT AND PROSPECTS OF DEVELOPMENT

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The Government of the Russian Federation has initiated a draft law which establishes the right of regions to introduce tax holidays for individuals. The privilege is expected to be granted to those who start business in production, social and scientific spheres. It is expected that the law in question will contribute to structural development of the small business at the expense of special support of those lines of business which are the most required at present in economic terms. At the same time, the draft law's concept of motivation of certain types of business activities could receive further development. In our view, provisions as regards the extent of application of tax holidays need to be updated.

Late in October 2014, the Government of the Russian Federation submitted for consideration to the State Duma of the Russian Federation the draft law establishing the right of regions to introduce tax holidays for individuals who made a decision to start their own business with use of a simplified or patent system of taxation provided that a switch-over to either regime took place within two years from the day of registration of the individual with tax authorities as an individual entrepreneur¹. Privileged tax conditions will consist in application of a zero tax rate to the income received by the individual, that is, actually full exemption of that income from taxation within one or two tax periods by decision of a constituent entity of the Russian Federation. Tax privileges are expected to be granted only to those entrepreneurs who start business in production, social and scientific spheres. The above measure is aimed at motivation of the small business (micro-business) and assists it in its structural development at the expense of special support of those lines of business which are the most required in economic terms at present. In addition to the right to introduce the rate, in case of approval of the draft law regions will have an opportunity to update the terms of application of that rate in practice. What is meant here is limitations regarding the average number of workers and the ultimate size of revenues received from sales.

As tax holidays are meant for those who are going to start their business and do not work as business entrepreneurs at present, no drop in budget revenues is expected. In addition to the above, tax holidays are going to be introduced on a temporary basis for the period till 2020.

It is to be noted that the above measure is implementation of one of the lines of the internal policy of the Russian Federation specified by President V. Putin

in his address to the Federal Assembly in 2013. It is to be reminded that at that time President V. Putin officially supported the idea that regions could “provide two-year tax holidays to newly-established small businesses operating in production, social and scientific spheres”².

In our view, the decision to support the small business is a timely and required measure for the government and the public. According to the data of the Rosstat, the number of actually operating individual entrepreneurs is still not very high: in 2013 their total number amounted to no more than 2.5m in Russia; it is to be noted that the dynamics of changes leaves much to be desired: 2.7m entrepreneurs in 2008 against 2.6m entrepreneurs in 2012. In other words, there is a risk that people are getting less and less interested in engaging in small business.

In addition to the above, there is always a problem related to the structure of the small business whose representatives normally prefer to engage in commerce as the most profitable and simple line of business in terms of economic benefits. On the basis of the results of 2013, it was registered that nearly 50% of all the entrepreneurs engaged in wholesale and retail trade, while less than 5% of them, in manufacturing.

At the same time, the draft law's concept of motivation of certain types of activities – which concept is aimed at solution of the problem of diversification of the micro-business – could receive further development. In our view, it is important to update provisions as regards the extent of application of tax holidays. As was stated, tax holidays are not available to those who already operate on the market and receive profit. At the same time, taking into account an explicit motivation and strictly target nature of that measure, that is, its aim to support innovations, production and social services, it is not quite clear what other businessmen

¹ Draft Law No.634370-6 on Amendment of Article 346-20 and Chapter 26-5 of the Tax Code of the Russian Federation.

² The Address of the President of the Russian Federation to the Federal Assembly on December 12, 2013.

who have already been registered as individual entrepreneurs will do if they want to start their business from scratch, that is, in the area in which they did not work before, for example, production. The proposed concept of amendments includes a situation where the right to a tax privilege could be granted to a person who started his business earlier, but took a decision to carry out another line of business in respect of which a tax privilege can be granted only to those individual entrepreneurs who were not registered before. The proposed limitation, that is, on the basis of the fact of the first registration of an individual as an individual entrepreneur does not permit to extend the new motivation onto such businessmen.

With application of the zero tax rate limited only to "new" individual entrepreneurs, the measure in question does not represent a potential of positive changes in the pattern of the population which already works as individual entrepreneurs. So, changes in the pattern can be achieved only by means of the influx of new persons and thus change the shares of entrepreneurs by the type of business activities. However, the proposed measure could become a good motivation for business people to start another more required business which situation is going to have a positive effect on the quality of development of the small business in Russia. So, it would be expedient to switch over from the principle of provision of the zero tax rate (tax holidays) on the basis of the fact of the first registration of an individual as the individual entrepreneur to provision of tax privileges in reorientation and conversion of the business into the field of production, science or social services, that is, those types of activities which were specified by the President in his address because in such a case business can be regarded as a new one.

In addition to the above, the procedure for switching over by a businessman to tax holidays is to be speci-

fied. Tax holidays are granted provided that a businessman is on a special tax regime and for that reason tax holidays are a kind of a privilege within the privileged tax regime or private tax regime within the frameworks of a simplified/patent system of taxation. Another condition for tax holidays is the fact that the businessman engages in the above lines of business. However, it is not specified in the draft law from which date the businessman should carry out activities in production, social and scientific spheres in order to receive the right to tax holidays: such a date can be either the date of registration of the individual entrepreneur or the date of a switch-over to a special tax regime. In either case, a person can be recognized as businessman carrying out the specified type of activities. It remains unclear whether in accordance with the draft law a businessman should work immediately in one of the above areas or he/she has the right after his/her first registration with the tax authorities to change the line of business before switching over to the special tax regime because a condition for a switchover to tax holidays is application of the special tax regime and the businessman has to account to tax authorities on the basis of the fact of application of tax privileges for compliance with the type of activities only for the period the special regime was applied. The above issue should be solved before amendment of the Tax Code of the Russian Federation because without doing that there is a high risk of different interpretations of the rules of application of tax holidays. In our view, the above problem can be solved by means of introduction of a provision that from the date of registration the person should immediately carry out one of the above types of activities, otherwise, such a businessman is in no way different from those who started their business earlier and in respect of whom that privilege was not initially applied to. ●