

#13 | May 2010

Reduced Russian Personal Income Tax Rates for Non-Residents

Generally, Russian individual taxation rules are distinguished by their comparatively low tax rates and the absence of a progressive taxation scale (as opposed to the majority of European countries). While the second issue is permanently under discussion by the Russian state authorities¹, it is unlikely that the first one will change in the near future. Moreover, new Federal Law No. 86-FZ dated 19 May 2010 "On amendments to the Federal Law "On the legal status of foreign citizens in the Russian Federation" and certain legislative acts of the Russian Federation" (hereinafter – the "Law") even provides for new, reduced, rates of personal income tax for several categories of Russian non-residents.

As a reminder, Russian personal income tax is levied on either tax residents (individuals physically present in Russia for at least 183 calendar days during a 12-month rolling period) or non tax residents. In this context, Russian tax residents are taxed on their worldwide income, and non-residents have tax imposed on their Russian-sourced income only, irrespective of the nature of that income.

The income tax regime for tax residents is generally more favourable than the one for non-residents. In particular, the following personal income tax rates are currently fixed in *Part II of the Russian Tax Code* No. 117-FZ of 5 August 2000 (hereinafter – the "Tax Code"):

Type of income	Rate
<u>Residents</u>	
All types of worldwide income, save for exceptions, as below	13% (general)
Dividends from Russian/foreign sources	9%
Prizes and awards received in contests, competitions and other advertising events (in excess of RUB 4000 (approximately EUR 104 ²))	35%
Interest income on bank deposits in excess of 9% per annum for deposits in a foreign currency and in excess of the refinancing rate ³ +5% per annum for deposits in rubles	
Economy on interest on received loans or credits in excess of 9% per annum for loans/credits in a foreign currency and in excess of the refinancing rate*2/3 per annum for loans/credits in rubles	
<u>Non-residents</u>	
All types of Russian-sourced income, save for exceptions, as below	30% (general)
Dividends from Russian sources	15% ⁴

The Law (generally based on the changes to migration legislation) improves substantially the income tax rates for non-residents. From now on the **13% personal income tax rate will apply to remuneration received from professional activities of non-residents regarded as "highly qualified" specialists.**

¹ For instance, a draft law proposing to decrease the personal income tax rate to 5% for individuals with a yearly income of less than RUB 60,000 (approx. EUR 1,558) and its increase to 45% for individuals receiving annual remuneration above RUB 12 m. (approx. EUR 311,690) is currently being discussed by the relevant ministries.

² Please note that for the EUR equivalents we have used the following exchange rate in the present Tax Outlook: EUR 1 = RUB 38,5.

³ Is equal to 8% per annum from 30 April 2010 (Instruction of the Russian Central Bank No. 2439-U dated 29 April 2010).

⁴ Unless otherwise provided for in double tax treaties concluded by the Russian Federation.

According to the Law, a foreign specialist will be considered as “*highly qualified*” if he obtained work experience, skills in a particular sphere⁵, and his professional activities in the Russian Federation are remunerated with a gross salary of at least RUB 2 m. (approx. EUR 51,950) per year. The following will be entitled to the benefit of the “highly qualified” status of foreign specialists and be able to apply the reduced tax rates: Russian commercial organisations, Russian non-commercial organisations undertaking scientific, technical, innovation activities and experimental trials, and branches of foreign legal entities⁶ not subject to administrative penalties for illegal employment of foreign citizens for the two years preceding the date of application for the “highly qualified” specialist employment status.

The Law also provides for 13% personal income tax rate for remuneration paid to non-residents that are not subject to the Russian visa regime and are employed in the Russian Federation by individuals on the basis of an employment agreement or a civil law contract for personal purposes not related to business activities. We believe that in practice this provision may be applicable to e.g. the services of nurses, housemaids and house building activities for personal purposes.

In general, these kinds of employees will be exempted from the obligation to receive work permits and will be able to buy so-called “*patents*” for the right to work in Russia. The price of such patents amounts to RUB 1,000 (approx. EUR 26) per month and its payment will be considered as an advance personal income tax payment. This means that foreign employees hired by individuals for personal purposes will be obliged to pay personal income tax not covered by the price of the patent (i.e. on the amount of their annual gross remuneration in excess of RUB 7,692 (approx. EUR 200)).

Finally, please note that although the modifications to the tax legislation introduced by the Law entered into force on the day of its official publication (on 21 May 2010)⁷, these new regulations will only be applicable from 1 July 2010.

Please also note that we will provide you with more detailed information on the fundamental legal changes to the Russian immigration regulations touched upon in the current CMS Tax Outlook in the forthcoming CMS Client Alert.

CMS can offer you the following assistance:

- Implementing new and/or revising your existing remuneration/HR policies and structures with a view to tax optimization (i.e. cost reduction) of personal income tax, company profits tax and social contributions
- Drafting and/or review of labour agreements and associated documentation of your company from both tax and legal points of view and assistance in negotiations to achieve more favorable terms
- Preparation and selection of documentation requested by tax inspectorates to justify remuneration expenses, calculated tax bases etc.
- Assistance in negotiation with the Russian tax authorities, to achieve early tax settlements and resolution of pending issues
- Representation of your company in disputes with tax authorities

If you have any questions on the matters referred to in this **RUSSIA TAX OUTLOOK**, please do not hesitate to contact Dominique Tissot, Partner, and Anastasia Prozor, Associate, or your regular contact at CMS, Russia.

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⁵ The relevant experience, competence and level of qualification will be evaluated solely by the employer (or customer) at his own discretion and risk.

⁶ Please note that Russian representative offices of foreign legal entities will not be entitled to employ foreign specialists subject to “highly qualified” specialist status.

⁷ The majority of migration-related provisions provided for by the Law should enter into force on 1 July 2010.

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