

#9 | December 2009 – January 2010

## Major Amendments to Russian Tax Legislation Coming into Force in 2010

In order to sum up the key developments in tax legislation during 2009, we have decided to devote our “transitional” 2009-2010 Russia Tax Outlook to all major amendments to Russian tax legislation (and primarily to the Tax Code of Russian Federation (Part I No. 146-FZ dated 31 July 1998 and Part II No. 117-FZ dated 5 August 2000)) which enter into force in 2010 and may substantially impact your businesses. It is going to be important to pay attention to these amendments in order to optimise the costs of your company, modify tax policy, plan further investments, conclude contracts with partners, etc.

### Accelerated Value-Added Tax Recovery

*(Federal Law “On Amending Part I and Part II of the Tax Code of the Russian Federation in Connection with Application-Based VAT Recovery Procedure Introduction” No. 318-FZ dated 17 December 2009 (referred to as the “Law” in the present section))*

VAT recovery is one of the most important and most troublesome aspects of the Russian tax system. The process of obtaining a refund of VAT in Russia is slow and requires substantial effort from the taxpayer. Until recently the process for obtaining a decision on VAT recovery by the Russian tax authorities took at least **three months** including the time required for carrying out the in-house tax audit on the submitted tax return.

To ameliorate the problem, a simplified VAT recovery procedure has been introduced which entitles a taxpayer to **recover VAT before completing the tax audit** and prior to a final decision on VAT recovery being adopted by the tax authorities. The new provisions of the Law on application-based VAT recovery came into force with effect from 1 January 2010 and apply to tax returns submitted for tax periods starting from the first quarter of 2010.

As a general rule, all taxpayers wishing to benefit from the accelerated VAT recovery procedure will be obliged to submit a proof of their financial solvency to the tax authorities, *i.e.* a **bank guarantee** whereby a bank<sup>1</sup> undertakes to pay tax arrears for the relevant taxpayer together with penalties and default interest if the taxpayer has recovered VAT unlawfully. A taxpayer may be exempt from this obligation only if:

- the aggregate amount of VAT, excise, profits tax and mineral resources extraction tax paid by him (excluding tax paid as a tax agent and tax paid in connection with the goods transferring across the Russian border) for the 3 prior calendar years is at least RUR 10 bln. (approx. EUR 227 mln.), and
- the taxpayer has existed for at least 3 years before the date of the claim for VAT recovery.

According to the new rules, the “accelerated” VAT recovery procedure can be concluded within **11 days**. The process will comprise the following stages: (i) submitting an application for VAT refund/offset during the period of 5 days following the respective VAT return filing; (ii) examination of the application by tax authorities within 5 days and adoption of a decision to recover VAT/ refuse the simplified VAT recovery; and (iii) VAT recovery. In cases of a failure to comply with the time limits for VAT recovery by tax authorities, interest (at a rate equal to the refinancing rate of the Russian Central Bank (currently 8,75 %<sup>2</sup>)) on the overdue recovery amount will accrue - this is an additional guarantee of taxpayers' rights.

Please note that this simplified procedure **does not abolish the in-house tax audit** necessary for the adoption of a final decision by the tax authorities to allow VAT recovery. The audit is still required and tax authorities will be entitled to challenge corresponding amounts. If the VAT sum recovered by a taxpayer exceeds the sum which is finally determined following the tax audit results, tax authorities will cancel the decision on the application-based VAT recovery (in full or in part) and such taxpayer will be obliged to return to the federal budget any excess amount recovered, together with **penalties accrued from the date when such taxpayer had received the relevant sums**.

<sup>1</sup> Only banks satisfying specific conditions (*e.g.* registered charter capital not less than RUR 500 mln. (approx. EUR 11.4 mln.), own funds not less than RUR 1 bln. (approx. EUR 22.7 mln.)) and included in a special list created by the Russian Ministry of Finance will be entitled to issue such bank guarantees.

<sup>2</sup> According to the Indication of the Central Bank of the Russian Federation No. 2369-U dated 25 December 2009 this refinancing rate is in act starting from 28 December 2009.

## Changes to Company Profits Tax

(Federal Law "On Amending Part II of the Tax Code of the Russian Federation and Federal Law "On Amending Chapters 23 and 25 of the Tax Code of the Russian Federation" and Recognising Several Provisions of the Laws of the Russian Federation Invalid" No. 368-FZ dated 27 December 2009 (referred to as the "Law" in the present section))

The "tradition" of the Russian legislative authorities introducing important new laws at the very end of the year was continued in 2009, and this unanticipated legislation was signed on 27 December. The new law principally concerns two issues: (i) **temporary** rules aimed at improving a taxpayer's position during a period of financial recession by providing for an increase to the threshold amount of interest on debt obligations and (ii) modification of the **taxation regime of dividends** received by Russian legal entities.

### 1. Increase to the threshold amount of interest on debt obligations

Under art. 269 (1) of the Russian Tax Code, as a general rule interest on loans and other borrowings in Russia is subject to limitations on profits tax deductibility and must be charged at a rate which is not more than 20% above the average rate charged for comparable loans made in the same quarter. In the absence of comparable data or at the taxpayer's choice, the maximum rate is as follows:

- for rouble loans, the refinancing rate of the Russian Central Bank at the date the loan is provided, multiplied by 1,1; and
- 15% for foreign currency loans.

However, these rules had been suspended for the period **from 1 September 2009 to 31 December 2009**: a maximum rate of the refinancing rate of the Central Bank multiplied by 2 for rouble loans and a maximum rate of 22% for foreign currency loans applied. Further, state legislative authorities have iteratively suspended the relevant provision of art. 269 (1) and have established that **during the period from 1 January 2010 to 30 June 2010** a maximum rate of the **refinancing rate of the Central Bank multiplied by 2 for rouble loans** and a maximum rate of **15% for foreign currency loans** shall apply for interest expenses on debt obligations arising **before 1 November 2009**. These new rules represent a temporary concession and the thresholds on loans will most likely be returned to the original rates fixed in art. 269 (1) as soon as the country emerges out of recession.

### 2. Taxation of dividends received by Russian companies

According to the Russian tax rules, dividends received by a Russian company from another Russian company or from a foreign legal entity are in principle taxed at a flat rate of 9%. However, dividends could be previously exempt from Russian corporate profits tax if the following criteria were met:

- the recipient of dividends held at least 50% of the charter capital of the dividends' payer<sup>3</sup> or owned depository receipts entitling it to receive at least 50% of the amount of paid dividends;
- the share or depository receipts had been owned for at least 365 days on the day dividends were declared; and
- the value of the investment was at least RUR 500 mln. (approx. EUR 11.4 mln.).

According to the new Law, **the condition as to minimum investment value of RUR 500 mln) has been abolished**. This change of the dividends' taxation regime is of particular importance for small and medium-sized companies and offers opportunities for Russian companies having subsidiaries in other countries.

Please note that the amendment will apply from **1 January 2011** and will cover relations arising after 1 January 2010, *i.e.* dividends arising on profits in 2010 onwards.

<sup>3</sup> Dividends from companies residing in low-tax jurisdictions (a list of these jurisdictions is being published by the Ministry of Finance) cannot be exempted from Russian corporate profits tax.

## Amendments Relating to the Taxation of Financial Instruments of Forward Transactions and REPO Transactions

(Federal Law "On Amending Part I and II of the Russian Tax Code and Certain Legislative Acts of the Russian Federation" dated No. 281-FZ 25 November 2009 (referred to as the "Law" in the present section))

The Law introduces a large number of amendments in respect of taxation of transactions involving financial instruments of forward transactions (hereinafter – "FIFT") and REPO transactions. These amendments concern primarily corporate profits tax (e.g. establishment of special rules for securities lending operations taxation and for the determination of income and expenses of clearing companies), VAT (e.g. introduction of VAT exemption rules for FIFT transactions (except for selling assets which are subject to VAT), securities loan operations, REPO transactions etc.) and personal income tax (e.g. new provisions concerning the procedure for determining the tax base for calculation of material gain resulting from the acquisition of FIFT).

If you require a more detailed analysis of these Russian tax legislation amendments, please refer to our *CMS Legal Digest for December 2009*.

## Change of the Transport Tax Rates and Indexation of Excises

(Federal Law "On Amending Chapters 22 and 28 of Part II of the Tax Code of the Russian Federation" No. 282-FZ dated 28 November 2009 (referred to as the "Law" in the present section))

The Law brings together into one document, two main aspects of tax legislation (transport tax and excise tax).

### 1. Transport tax issues

Transport tax rates reform was a hotly debated matter during 2009. Several Drafts on the issue were examined by the Russian Parliament. However, even the final version adopted at the end of November displeased the majority of car owners who organised several mass protests.

The general rules of application for transport tax are established by the Russian Tax Code. According to the current legislation, transport tax is a regional tax assessed on registered transportation vehicles and payable by the registered owner. The procedure for collection and filing of the relevant tax return is established regionally. Current transport tax rates were introduced to the Russian Tax Code in 2003 and depend primarily on a vehicle's engine capacity.

Initially, the idea of the reform was to double current transport tax rates and to grant the right to the regions of the Russian Federation to increase these new rates by up to ten-fold. Notwithstanding the fact that the new Law was only supported by "Edinaya Rossiya" and three out of the four parties represented in the Russian Parliament voted against the adoption of the Law, the Draft Law was adopted by the State Duma. The Federation Council, however, has rejected the Draft and created a conciliation commission jointly with the Duma.

The final version of the Law leaves the standard transport tax rates established by the Tax Code unchanged but grants regional authorities scope to **increase/decrease transport tax rates by up to 10 times** (instead of former 5 times) **with the possibility to establish variable rates according to the age and/or emission class of vehicles**.

Some regions have already confirmed their plans to increase transport tax rates. Kirov, for example (by 1,5-2 times), Chechnya, Krasnodar and Perm regions (up to 10-15%), Tatarstan and Kaliningrad (up to 25%). The situation in Moscow and St. Petersburg is the opposite: the competent authorities announced that rates will not be increased in the short term<sup>4</sup>.

<sup>4</sup> Currently, in Moscow the minimum transport tax rate for vehicles with an engine not exceeding 100 hp is equal to RUR 7 (approx. EUR 0.16) per 1 hp (whereas the standard rate is RUR 5 (approx. EUR 0.11)), the maximum rate, for vehicles exceeding 250 hp, – RUR 150 (approx. EUR 3.4) (standard rate – RUR 30 (approx. EUR 0.68)) and in St. Petersburg – RUR 10.5 (approx. EUR 0.24) and RUR 100 (approx. EUR 2.27), respectively.

## 2. Excise tax

The Law substantially increases excise tax rates for several types of goods, especially, ethanol, beer, tobacco goods, motor cars, engine oil and petrol. For example, the excise tax for alcoholic goods with an alcoholic percentage exceeding 9% will be increased by 20%, excise for tobacco products by 40% and for beer with an alcoholic percentage of 0.5% up to 8.6% – by 300%.

### Replacement of the Unified Social Tax with Insurance Contributions

(Federal Law “On Insurance Contributions to the Pension Fund, Social Security Fund, Mandatory Medical Insurance Fund and Territorial Mandatory Medical Insurance Funds” No. 212-FZ dated 24 July 2009 (referred to as the “**Law**” in the present section))

Up to the end of 2009, employers in Russia were subject to the unified social tax (UST) which was assessed on an employee’s annual remuneration. The UST payments were made on a regressive scale with a 26% general rate.

However, under the new Law which entered into force on 1 January 2010, UST is now replaced with insurance contributions payable to four separate state non-budgetary funds: the Pension Fund, the Federal Social Security Fund, the Federal Mandatory Medical Insurance Fund and the Territorial Mandatory Medical Insurance Fund. Moreover, it cancels the regressive scale and increases the general tax rate to **34% for the part of remuneration below RUR 415,000 (approx. EUR 9,432)**.

From 1 January 2010 to 31 December 2010 a transitional period will operate during which the general rate will remain unchanged (*i.e.*, a 26% rate will apply to any pay below RUR 415,000). Additionally, some tax privileges under the Tax Code will be preserved during this period (*e.g.*, companies operating the simplified taxation system will pay insurance contributions at a general rate of 14%).

Moreover, the Law provides for the **exemption of payments and other compensations paid under employment and civil contacts in favour of foreign citizens (stateless persons) temporarily located** on the territory of the Russian Federation. This means that foreign citizens who arrive on the Russian territory on the basis of a visa (or without a visa in cases where one is not required) and receive a migration card but do not have a residence permit or a temporary living permit, are exempted from all types of social contributions to be paid to the Russian non-budgetary funds.

For more information on this key reform of the Russian tax legislation, please refer to *CMS Tax Outlook #5 of July-August 2009 “Anticipated Reform of Unified Social Tax: Impact on Businesses?”*

### Amendments to the Tax Code in the Sphere of Energy Efficiency and Energy Saving

(Federal Law “On Energy Saving and Energy Efficiency Increase and Amending Certain Legislative Acts of the Russian Federation” No. 261-FZ dated 23 November 2009 (referred to as the “**Law**” in the present section))

The main declared objectives of the Law are to promote the efficient use of energy resources, to give support and encouragement to energy saving (ES) and to increase energy efficiency (EE), as well as to promote planning and integration of activities increasing EE. In addition, the Law codifies measures aimed at rewarding ES implemented by the general public, businesses and the public sector, notably through the use of tax and budget incentives as well as improved tariff policies.

The tax incentives include, in particular, investment tax credits up to 30% for companies investing in EE and ES technologies, accelerated depreciation of assets belonging to the category of objects with high EE or sites classified in top EE classes and partial compensation of interest on loans granted by Russian banks for the purpose of investing in ES and increased EE technologies.

For more information, please refer to our *CMS Tax Outlook #8 of November 2009 “Tax Aspects of New Energy Efficiency Legislation in Russia”*.

## “Decriminalisation” of the Tax Liability

*(Federal Law “On Amendments to Part 1 of the Tax Code of the Russian Federation and Certain Regulations of the Russian Federation” No. 383-FZ dated 29 December 2009 (referred to as the “Law” in the present section))*

The Law relaxes the criminal liability regime for tax offences and makes amendments to the Criminal Code No. 63-FZ dated 13 June 1996, the Code of Criminal Procedures No. 174-FZ dated 18 December 2001 and the Tax Code. These measures have been widely debated in mass media, business sector and public bodies. The Law was finally signed by the President just prior to the end of 2009 and the majority of its provisions are in effect from 1 January 2010.

The Law increases substantially the **thresholds (unpaid tax amounts) giving rise to criminal liability for tax offences**, as follows:

- for individuals – RUR 600,000 (approx. EUR 13,640) during 3 financial years provided that the portion of unpaid taxes represents at least 10% of the sum due, or RUR 1,800,000 (approx. EUR 40,910) (formerly – RUR 100,000 (approx. EUR 2,270) during 3 financial years and RUR 300,000 (approx. EUR 6,820), respectively); and
- for companies – RUR 2,000,000 (approx. EUR 45,450) during 3 financial years provided that the portion of unpaid taxes represents at least 10% of the sum due, or RUR 6,000,000 (approx. EUR 136,360) (formerly – RUR 500,000 (approx. EUR 11,360) during 3 financial years and RUR 1,500,000 (approx. EUR 34,090), respectively).

According to the Law, the taxation authorities must **notify taxpayers of threatened criminal prosecution** against them. The taxpayer should not be subject to criminal liability if he/it pays the arrears of tax, together with default interest and penalties claimed in accordance with a taxation authority’s notification. The Law additionally provides that a taxpayer can only be held criminally liable for a tax offence which infringes, and occurs after, a taxation authority’s decision which has become effective.

The Law gives an option to escape punishment and to be exempted from criminal liability also when a criminal case is at a pre-trial stage. This is conditional upon, first, the damage caused to the state being repaired voluntarily and in full and, second, the taxpayer being in tax arrears for the first time.

Finally, the Law provides for the modes of **information exchange between the tax authorities and the territorial departments of the Russian Ministry of internal affairs**. If a taxpayer fails to pay tax arrears, penalties and fines in full within two months from the date specified in the tax payment notice the tax authorities have 10 days from the moment they become aware of the default, to send relevant materials to internal affairs departments. It is the departments of internal affairs that decide whether or not to initiate criminal proceedings against such taxpayers.

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.

### CMS, RUSSIA

DOMINIQUE TISSOT  
DOMINIQUE.TISSOT@CMSLEGAL.RU

ANASTASIA PROZOR  
ANASTASIA.PROZOR@CMSLEGAL.RU

Gogolevsky Blvd, 11  
119019, Moscow  
T +7 495 786 4000  
F +7 495 786 4001  
[www.cmslegal.ru](http://www.cmslegal.ru)