

#15 | August 2010

## Ministry of Finance Clarifies Rules on the Taxation of Highly Qualified Specialists

New, reduced rates of personal income tax for several categories of Russian non-residents<sup>1</sup> are applicable from 1 July 2010. Notably, the Russian Tax Code (Part II No. 117-FZ of 5 August 2000 – the “**Tax Code**”) now stipulates that the 13% personal income tax rate applies to income received from professional activities of non-residents regarded as “*highly qualified specialists*”, instead of the former 30% tax rate that was applicable to all Russian-sourced income of non-residents.

However, there are some practical issues raised by the new rules on the taxation of highly qualified specialists. For instance, it is not absolutely clear as to what categories of a specialist’s professional income the 13% rate may apply. In practice, therefore, this question may lead to disputes both between the employer and a highly qualified specialist employee, as well as between the tax authorities and the employer acting as the tax agent of such an employee. A new Letter of the Russian Ministry of Finance No. 03-04-06/0-181 dated 17 August 2010 (the “**Letter**”), seeks to clarify this issue as follows.

According to the 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”, introducing a new category of foreign employees, a highly qualified specialist is a foreign employee having professional skills, knowledge and qualifications in a specific area<sup>2</sup>. In addition, such an employee should be remunerated with a gross salary of at least RUR 2 million within a one year period (*i.e.* approximately EUR 50,891 per year or EUR 4,241 per month).

As indicated above, Russian non-residents employed as highly qualified specialists are entitled to the 13% personal income tax rate in respect of their **income received from professional activities**. This wording of the Tax Code gives rise to three main interpretations:

- The 13% rate is applicable solely to the salary of the employee; or
- The 13% rate is applicable to all payments specified in the employment agreement with the highly qualified specialist (including, for instance, compensation of the accommodation costs (apartment rental), costs related to visa support, payments for the insurance of property interests of the employee); or
- The 13% rate is applicable to all payments received by such an employee from the employer, irrespective of the fact of their indication in the employment agreement.

According to the position expressed by the Russian Ministry of Finance in the Letter, **the 13% personal income tax rate applies solely to the salary of the highly qualified specialists**.

Given that, please note that according to the Labour Code of the Russian Federation No. 197-FZ dated 30 December 2001, an employee’s salary includes (i) remuneration; (ii) stimulation payments (rewards, bonuses, additional payments and increases of a stimulating character as well as other incentive

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<sup>1</sup> Generally, 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.

<sup>2</sup> The relevant experience, competence and level of qualification should be evaluated solely by the employer at his own discretion and risk on the basis of authentic documentation. The documentation may also be reviewed by the migration service upon verifying the application for the status of a highly qualified specialist.

payments); and (iii) compensational payments provided for by the legislation of the Russian Federation (e.g. payments for work in extreme weather conditions).

For more information on the concession of the status of a highly qualified specialist and the taxation of this category of non-residents, please refer to our CMS Tax Outlook “Reduced Russian Personal Income Tax Rates for Non-Residents” of May 2010 and the CMS Legal Alert “Amendments to the migration legislation, effective from 1 July 2010” of June 2010.

**CMS can offer you the following assistance:**

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

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

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