Corporate income tax subjects - 2013 EATLP Congress

Russian National Report

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1. General presentation

1.1. Overview of the system

1.1.1. Russian tax legislation does not use the term "Corporate income tax". In the period from 1991 to 2002 the respective tax was known as "Tax on profit of organizations and enterprises", since 2002 – as "Tax on profit of organizations".

Thus, one of the important features of the Russian system of profit taxation is that the definition of the term "corporation" is not so relevant for profit taxation. In accordance with the Russian approach all kinds of "legal persons"[1] (we may oppose this term to the term "natural persons") may be regarded as taxpayers of Tax on profit of organizations.

The traditional discussions on a tax distinction between corporations and partnerships are not typical for the academic literature and practice in Russia. The issues "opacity vs. transparence", in fact, should be solved exclusively in the framework of Russian civil legislation.

In particular, Articles 69 – 81 of the RF Civil Code provide for the possibility to create a General Partnership as an autonomous legal person. Respectively, Article 69 (1) states:

"A partnership is considered general if its participants (general partners), in accordance with the agreement concluded between them, engage in entrepreneurial activities in the name of the partnership and bear liability for its obligations with the property belonging to them.

A person may be a participant in only one general partnership".

Additionally, Articles 82 – 86 of the RF Civil Code establish a "hybrid" form of legal persons – Partnership in Commendam. Article 82 (1) defines that:

"A partnership in commendam is a partnership in which, along with the participants conducting entrepreneurial activities in the name of the partnership and bearing liability for the obligations of the partnership with their property (general

[1] See: Article 48 of the RF Civil Code.

partners), there are one or several participants-investors (in commendam partners) who bear the risk of losses associated with the activities of the partnership within the limits of the sums of the investments contributed by them, and who do not participate in the conduct of entrepreneurial activities by the partnership."

On the contrary, partners may decide not to create a general partnership or a partnership in commendam (as autonomous legal persons) but just to conclude a Contract of Simple Partnership. Under the contract of simple partnership (contract of joint enterprise) two or more persons (partners)[2] undertake to pool their contributions and act jointly without creating a legal person in order to derive profit or accomplish another purpose not contrary to law (see: Article 1041 (1) of the RF Civil Code).[3]

Thus, the *issues "opacity vs. transparence"* in regard to Russian partnerships are predetermined by civil legislation and, in general, are not subject to tax law.

1.1.2. Tax on profit of organizations is a universal tax, i.e. it should be paid both by commercial and non-commercial organizations (in respect to the excess of income over expenditures of a non-commercial organization).

Small business may be exempted from tax on profit in case a respective legal person applies one of simplified regimes of taxation (Article 18 of the RF Tax Code).

Some companies activities of which are connected with extraction of natural recourses may be subject to tax on extraction of natural recourses (Chapter 26 of RF Tax Code). In regard to some kind of natural resources the tax base of this tax should be calculated in accordance with the rules similar to the respective rules of tax on profit (Chapter 25 of RF Tax Code).

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[2] Parties to the contract of simple partnership concluded for the purpose of conducting entrepreneurial activity may only be individual entrepreneurs and (or) commercial organizations – Article 1041 (2) of the RF Civil Code.

[3] It should be noted that since 1 July 2012 it is possible to create (in accordance with Federal Law of 3 December 2011 No 380-FZ "On economic partnership") a new type of partnership - "economic partnership". Though the "economic partnership" has a status of legal person, the partners may regulate their internal relations by a confidential civil contract which is not subject to the state registration (as it is usually provided for the Charter of legal person).

1.2. Historical evolution

Historically, we may see the prototypes of the modern system of corporate profit taxation even in the XIXth – the beginning of the XXth centuries. However, from the practical point of view it does not make sense to compare tax on trade and business enterprise (collected in the above-mentioned period) and modern tax on profit because the legislative technique and most of taxation rules are completely different.

Thus, for Russian academic literature on tax law the common approach is to consider the evolution of the system of profit taxation since 1991 (excluding also the soviet period of 1917 – 1991).

The instability of the Russian economy of the 1990-es caused some peculiarities of profit taxation. Since that period many representatives of business community consider establishing a corporation as an important instrument for restricting civil law liabilities. Taking into account this consideration we may explain why the setting up of a legal person should be recognized as an ordinary way of performing a business activity in Russia for big, medium and in many cases even for small business.

It is possible to illustrate our conclusion by statistic data (on 1 December 2012). In accordance with the official information of the Russian Federal Tax Service, there are 4,555,490 legal persons incorporated in the Russian jurisdiction (119,181 of them are under the liquidation procedures).[4] Among them 3,872,367 are the commercial organizations and only 358 and 536 of them are general partnerships and partnerships in commendam respectively.

[4] See : http://www.nalog.ru/gosreg/reg_ul/reg_ur_lic/.

2. Legislative technique

2.1. Sources

There is no special concept of “taxpayers of profit tax” in the RF Tax Code. In Chapter 25 “Tax on profit of organizations” and in Article 11 (the article is devoted to the definitions of terms and concepts which are used in tax legislations) of the RF Tax Code we may see just implicit or sometimes explicit references to civil legislation, i.e. any legal person recognized as such (according to civil legislation) should be regarded as a potential profit taxpayer.

2.1. Legal drafting

Article 11 (1) of the RF Tax Code provides for the general principle in accordance with which the terms and concepts coming from other branches of legislation (in this case from civil legislation) shall be understood in tax legislation as they are defined in those other branches of law.

Taking into account this approach it does not make sense for Russian legislator to introduce a special list of entities which fall under profit tax. The legislator rather provides for a general criterion and has made a reference to civil legislation (see the concept of legal person in Article 48 of the RF Civil Code).

3. Domestic entities

3.1. First approach

As it has been mentioned earlier, there is no accurate list of domestic entities which are subject to profit tax in the Russian Federation. However, it is possible to name the main forms of commercial and non-commercial organizations the creation of which is provided for by the RF Civil Code.

Commercial organizations (legal persons) may be formed as:

- General Partnership (Articles 69 – 81);
- Partnership in Commendam (Articles 82 – 86);
- Limited Liability Company (Articles 87 – 94);
- Supplementary Liability Company (Article 95);
- Joint Stock Company (Articles 96 – 104);
- Production Cooperatives (Articles 107 – 112);
- State and Municipal Unitary Enterprises (113 – 115).

Besides, all kinds of Non-Commercial organizations (see: Section 3.2.2 of the Report) may also be included in the list of taxpayers of profit tax.

A form in which a legal person has been created, as such, does not give any grounds for exemption from profit tax. Thus, it would not be methodologically correct to try to identify *general* futures of all domestic entities which are not subject to profit tax.

In principle, an exemption from profit tax in regard to certain types of entities may be provided for by tax legislation:

firstly, if these types of entities should not receive profits at all (for instance, for state bodies any economic activity is prohibited);

secondly, if some types of entities are involved in activities which are important for society and they may have a right for special tax exemptions or incentives provided for by Chapter 25 of the RF Tax Code (for instance, we may mention companies in charge of exercising the program of preparation for the Olympic Games in Sochi in 2014);

thirdly, if some companies have a status of residents of special economic areas and may apply for respective tax incentives (for instance, have a status of resident in "Skolkovo").

3.2. More details

3.2.1. Link between company law and tax law

As it was mentioned before, the definition of a person subject to profit tax fully depends upon company law definitions (the respective lists of entities and legal sources are included in Section 3.1 and 3.2.2 of the Report).

The RF Tax Code does not provide for a link between limited liability of shareholders (or partners) and the personal scope of profit tax. In particular, one-person companies should be subject to profit tax as any other companies.

For entities incorporated in accordance with Russian company law it is absolutely necessary to enjoy legal personality in order to be subject to profit tax. However, foreign entities without legal personality sometimes also have to pay profit tax – for instance, branches and representative offices (created on the Russian territory) of foreign companies (Article 11 (2) of the RF Tax Code, see Section 4 of the Report).

3.2.2. Charitable organizations and associations

A) Russian charitable organizations and associations. In general, all charitable organizations and associations may be subject to Russian profit tax. In this respect the Russian tax system uses the same approach and criteria to those used in the context of VAT liability. The above-mentioned approach is also applicable in regard to foreign entities; however, sometimes foreign entities may not enjoy exemptions from profit tax which are provided for by the RF Tax Code to residents.

It is important to note that, though there is no general ban for commercial organizations to conduct not for profit operations it is assumed that it is *non-commercial organizations* that have *a special legal status* engage in non-commercial activities. The civil legislation *does not intend to establish a closed list of their forms* (i.e., hypothetically, any special law, if it is necessary, might establish an additional

organizational form for non-commercial organizations). But their main forms are defined in Articles 6 – 11 of the Federal Law "On non-commercial organizations". They may be classified as follows:

- Social and religious organizations (associations) – (Article 6);

- Some traditional social and cultural associations, namely – associations of indigenous smaller nationalities of the Russian Federation (Article 6.1) and Cossack societies (Article 6.2);

- Foundations (Article 7);

- Special state agencies which may be divided into two groups according to a number of formal features and named by different (though quite similar in their meaning) terms – state corporations (Article 7.1) and state companies (Article 7.2);

- Non-commercial partnerships (Article 8);

- Institutions among which are: private institutions (Article 9) and public (state, municipal) institutions (Article 9.1). The latter, in their turn, are subdivided into autonomous, budget-supported and fiscal (Article 9.1 (2));

- Autonomous non-commercial organizations (Article 10);

- Amalgamation of legal persons (associations and unions) (Article 11);

- Consumer Cooperatives (Article 116 of the RF Civil Code).

All the above-mentioned forms of non-commercial organizations may significantly differ in what legislation establishes for the system of management (the procedure for managing an organization and creating its executive bodies), property rights of the members/participants/founders of an organization, etc. However, the form of a non-commercial organization is only of significance for tax regulation in a limited number of cases when it is directly established by the RF Tax Code (for instance, special preferential tax regimes for public budget-supported institutions).

B) Foreign charitable organizations and associations. Article 1 of the Law "On non-commercial organizations" states that it applies not only to all non-commercial organizations founded on the Russian territory (Article 1 (1)) but also establishes the compliance rules for the structural subdivisions (branches) of foreign

non-commercial and non-governmental organizations on the Russian territory (Article 1 (2.1)).

Russian legislation gives the definition of a "*foreign non-commercial organization*" in Article 2 (4) of the above-mentioned Law. This article states: "A foreign non-commercial non-governmental organization in this Federal Law is deemed to be an organization which does not have the making of profit as the primary purpose of its activities and does not distribute the profit received between the participants, which is founded outside the Russian territory in accordance with the legislation of a foreign state, and the founders of which are not the state authorities".

Russian legislation on non-commercial organizations assumes that if a foreign organization conducts its activity in Russia, it has to make its presence in the Russian Federation official in a certain way. Thus, Article 2 (5) of the Federal Law "On non-commercial organizations" states that a foreign non-commercial non-governmental organization conducts its activities on the Russian territory only through its structural (territorial) subdivisions – branches or representative offices. Articles 2 (2) and 2 (3) underline: "a structural (territorial) subdivision – a part of a foreign non-commercial non-governmental organization is recognized as an independent form of non-commercial organization and is subject to state registration in accordance with the procedure defined by Article 13.1 of this Federal Law".

Structural (territorial) subdivisions – branches and representative offices of foreign non-commercial non-governmental organizations acquire a legal subjectivity in the framework of the Russian legal system on the day the information about the respective structural (territorial) subdivision on the Russian territory is included, in accordance with the procedure provided for in Art.13.2 (3) of the Federal Law, into the list of the branches and representative offices of international and foreign non-commercial organizations. These provisions of the Law are quite peculiar, as in essence, assume giving the structural (territorial) subdivisions of foreign non-commercial organizations operating in the Russian Federation an independent legal status, that is equaling them (these subdivisions) in their status to domestic legal

entities (after going through an appropriate registration, namely as subdivisions, but not as legal entities)[5].

3.3.3. Miscellaneous on subjects of tax

Specific legal structures, e.g. trusts, silent partnerships may be used in Russian jurisdiction in accordance with the rules of private international law.

State-owned entities, as it was mentioned earlier, in general are subject to profit tax as other entities (with the exception to state bodies/authorities).

If companies belong to a **consolidated group of taxpayers** (registered in accordance with the RF Tax Code), they no longer enjoy full tax personality in the scope of profit taxation.

Taxpayers are able to apply for establishing a consolidated group of taxpayers from 1 January 2012 (Federal Law No 321-FZ of 16 November 2011). The RF Tax Code (amended by the above-mentioned Federal Law) provides for that a Consolidated Group of taxpayers is to be a voluntary association of profit taxpayers for the purposes of calculation and payment of profit tax based on the aggregate financial results of all Group participants. The agreement establishing the Group must be registered and accepted by the tax authorities. Only Russian companies can participate in Groups. The minimum period for which a Group may be established is two years. A Group may be established by companies if one company directly or indirectly holds at least a 90% share in the others.

The group of companies should satisfy the following main criteria on applying to establish a Group:

- the aggregate amount of federal taxes which must have been paid in the preceding calendar year was at least10 billion Rub.;

- the total revenue of the Group in the preceding calendar year was at least 100 billion Rub; and

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[5] See e.g. on this issue: *Borisov A. N.* Comments on the Federal Law "On non-commercial organizations", Moscow, Yustitzinform, 2007 (Comments to Art. 2).

- the aggregate value of assets of the Group as at the preceding 31 December was at least 300 billion Rub.

The law includes also other criteria, for example, the companies should not be undergoing reorganization, insolvency proceedings or liquidation and their net assets should exceed charter capital.

Tax accounting, tax calculation and tax payment responsibilities for the entire Group will be imposed on one participant, which is designated the “responsible participant”. Should this company fail to discharge its liabilities, all members of the Group will be liable jointly and severally for any tax underpayment, the corresponding penalties and late payment interest.

Transactions amongst participants of the Group are not subject to transfer pricing control (except for taxpayers of mineral extraction tax at ad valorem rates, such as those which extract precious metals, ferrous metals, and various types of salt).

The law does not exclude companies which have subdivisions outside Russia from participation in a Group.

3.3.4. Partial implementation

Limited Partnerships / Partnership in Commendam in Russia are subject to profit tax as other legal persons. Thus, they are considered opaque.

Partial implementation of profit taxation may be seen in some specific cases, for instance, in case of the simultaneous application of the general taxation regime (including tax on profit) and special taxation regime (single tax on presumed income in regard to some activities of small business).

3.3.5. Tax planning

In principle, the choice of legal structure is not a critical importance for tax planning purposes in the Russian jurisdiction. This point should be considered in connection with the purposes of economic activities and characteristics of transactions (civil law rules).

This Table illustrates the current situation (on 1 December 2012)[6]:

Number of legal persons incorporated in Russia	4,555,490
Including	
Commercial organizations	3,872,367
General Partnerships	358
Partnerships in Commendam	536
Limited Liability Companies and Supplementary Liability Companies	3,613,758
Joint Stock Companies	172,249
Production Cooperatives	18,181
State and Municipal Unitary Enterprises	11,293
Other commercial organizations	55,992
Non-commercial organizations	683 123
Consumer Cooperatives	80 170
Foundations	208 757
Legal persons which should be registered in accordance with the special procedure	271 713
Other non-commercial organizations	122 483

3.3.6 Others

Some profit tax rules have general effect and, thus, influence the calculation procedures in regard to other taxes. For instance, if in accordance with Article 306 (i.e. Chapter 25 "Tax on profit of organizations") the existence of permanent establishment was identified this legal conclusion is also important for calculating tax on property of organizations, VAT and etc.

[6] See : http://www.nalog.ru/gosreg/reg_ul/reg_ur_lic/.

4. Cross-border situations

4.1. If a foreign entity carries out business in Russian jurisdiction and has a *civil law capacity as autonomous entity in accordance with the respective foreign civil law*, it should be obviously considered as taxpayer in regard to profit tax.

Russian tax legislation does not provide for any "resemblance test" (i.e. the foreign entity may be subject to profit taxation, it is not relevant whether its features are comparable to those of domestic legal persons). In general, rules of the Russian private international law should be applied in this field.

4.2. In regard to cross-border situations some difficulties of another character may be identified.

The matter is the following: a structural subdivision of a foreign organization, *on the one hand*, is *a part of a foreign legal entity* (in accordance with the legislation of the country where this non-commercial organization is created)[7], *on the other hand*, is a person actually equaled to *an independent legal entity* in accordance with the Russian tax law.

Thus, the RF Tax Code follows this quite a controversial model of regulation established in Article 11. In particular, Article 11 of the RF Tax Code recognizes branches and representative offices of international and of foreign organizations (and also any other "corporate entities" having a civil capacity and created in accordance with legislation of foreign states) as autonomous participants of tax law relations, i.e. as independent taxpayers.

As it is known, Russia is not an EC Member-state. However, the Partnership Agreement concluded in 1994, ratified in 1997 and prolonged up till now, assumes the application of some fundamental freedoms between the Russian Federation and the EC in the sphere of economic activities.

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[7] In this respect, of interest is the phrasing of Art. 83 (3) of the RF Tax Code. According to it, the registration with tax authorities of a foreign organization is done at the place of conducting its activities on the Russian territory through its subdivision. So, it is not the subdivision of a non-commercial organization that is registered with tax authorities but the non-commercial organization itself (at the place of its subdivision's location).

Though the special status of structural (territorial) subdivisions of foreign organizations should not cause for them any obstacles of tax nature, which would contradict the Partnership Agreement (due to the fact that they actually fall under the national tax treatment), in a number of cases, however, some issues may arise in this sphere. They, in particular, may be connected with the following: the fact that though the structural (territorial) subdivisions of foreign non-commercial organizations are considered as the forms of legal entities, which are established according to Russian law, the interpretation of Article 11 of the RF Tax Code refers them to foreign organizations, i.e. *non-residents*.

This point does not always allow to clearly identify whether a resident or non-resident tax treatment should be applied in regard to them (if it is not specified in a particular provision of the RF Tax Code).