

**DOING
BUSINESS
IN**

RUSSIA



HLBRUSSIA

*doing business
in Russia*

foreword

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general information

LOCATION AND CLIMATE

The Russian Federation (Russia) is situated in the East of Europe and in the North of Asia. Russia is the largest country in the world covering 17.1 million square kilometres.

Russia has borders with 14 countries crossing 8 time zones.

Russia is surrounded by 12 seas and 3 oceans. The biggest mountain systems are the Urals, the Caucasus and the Altai mountains. The longest rivers are the Volga in Europe and the Lena and the Enisei in Asia. The largest lakes are Ladoga and lake Baikal.

The climate varies from arctic in the North to continental in the central part and subtropical in the South.

January temperatures in different parts of the country may range from 0 to -50 C. The average July temperature varies from +1 to +27 C.

The country possesses a wide array of natural resources including major deposits of oil, coal, and natural gas, many strategic minerals, diamonds, and timber.

CONSTITUTION AND POPULATION

The population of Russia is about 142.9 million people.

The capital of the Russian Federation is Moscow. With its 11.5 million population it is the largest city in the country, its principal economic and political centre - the seat of the President, the Government and the State Duma (Parliament).

St. Petersburg (formerly Leningrad) is the second largest city in Russia. Having about 4.9 million inhabitants it is an important cultural and industrial centre of Russia, the biggest transport junction of the country bordering Europe.

Others large cities are Rostov-on-Don, Nizhniy Novgorod, Ekaterinburg, Novosibirsk.

Russia is a federative republic as established by the 1993 Constitution. Administratively the Russian Federation consists of 83 federal regions including 21 republics, 9 krais (federal territories), 2 federal cities, 46 oblasts, 1 autonomous oblast and 4 autonomous areas. In order to centralise state internal and external policy all federal regions are united into 7 federal districts.

The structure of state power breaks down into three branches: legislative, executive, and judicial.

The President is elected for a six-year term on the basis of universal suffrage. He nominates members of the Government.

The President also heads the armed forces and the Security Council. The President has extensive veto powers over legislation introduced by the parliament, as well as an enhanced ability to generate legislation through executive power channels.

The legislative power is represented by the Federal Assembly consisting of the Federation Council and the State Duma.

CURRENCY AND LANGUAGE

Russian is the country's official language. Republics are empowered to set their own languages which are used along with Russian on their territories

The national currency is the Russian rouble (1 rouble = 100 kopecks)

LEGAL SYSTEM

The Russian legal structure is based upon statutory law (continental system) in contrast to common law (Anglo-Saxon system). A substantial part of Russian legislation regulating relations connected to business activities is codified, i.e. consists of codes of laws (Civil Code, Tax Code, Arbitral Code, etc.). Other legislation includes laws, Presidential decrees and governmental resolutions.

ECONOMY AND RESOURCES

Following the collapse of the Soviet Union in 1991, Russia is implementing reforms aimed at transforming its centrally planned economy into a free market system. As a result of giving up the planned economy state-owned businesses were privatised, state controls on prices were abolished and a banking system and stock and commodity exchanges were established.

In majority opinion, the rates of free-market economy development and reform in the Russian Federation were comparable with those of China. Nevertheless certain problems mainly concerned with the low standard of living still exist and are being overcome.

Today the Russian economy is based traditionally on heavy industry, extractive industry, and agriculture. Russia is a major producer of chemicals, iron, steel, cement, timber, electricity, and coal. In addition service industries are developing.

The biggest centres of extractive industry are in following regions:

- mineral oil deposits: Western Siberian and Volgo-Urals oil areas;
- gas deposits: Kuznetskiy, Pechorskiy, and Kansko-Achinskiy basins. Russia possesses roughly one third of the world's natural gas reserves and currently supplies one fourth of all gas on the world market;
- ironstone deposits: the Kursk magnetic anomaly, the Urals, and Western Siberia
- ferrous metallurgy: Magnitogorsk, Chelyabinsk, Nizhniy Tagil, Novokuznetsk, Cherepovets, and Lipetsk;
- non-ferrous metallurgy: Norilsk, Krasnoyarsk, and Irkutsk

Russian mineral deposits also include gold, silver, platinum, cobalt, antimony, zinc, mercury, and many others.

Centres of engineering industry are located in Moscow, St. Petersburg, Urals, and Western Siberia. Major chemical plants are settled in the North-West and Central regions, and in the Urals. The woodworking industry is based in East and North of Russia.

Russia's electrical power infrastructure consists of generating equipment with an output of more than 200 million kilowatts, 45 thousand kilometres of high voltage grid, and 2,700 thousand kilometres of low voltage grid. It represents the largest electrical supply structure in the world.

The centres of agriculture are situated in the Central region, the Black Earth zone, North Caucasus, and Western Siberia. Staple crops are grain-crops, white beet, sunflower, flax, and potatoes.

Route miles of the Russian railways are more than 152 thousand kilometres, the length of trunk pipelines amount to 206 thousand kilometres, highways 949 thousand kilometres, internal waterways 101 thousand kilometres.

The most important ports are seaports in St. Petersburg, Vanino, Novorossiysk, Murmansk, and Kaliningrad.

Major transport junctions are Moscow, St. Petersburg, Novosibirsk, and Khabarovsk.

INTERNATIONAL ECONOMIC LINKS AND MEMBERSHIP OF INTERNATIONAL TRADE ORGANISATIONS

Russia has extensive economic links with many countries. International trading volumes in 2011 totalled 845.2 billion USD. of which import volumes were at 323.2 billion USD and export volumes were at 522.0 billion USD. Among the most significant trading partners of the Russian Federation are the European Union (about 48.0% of trade volumes), the CIS countries (14.9% of trade volumes) and countries of the Asia-Pacific Economic Cooperation (23.9% of trade volumes). Russia imports machinery, food, chemicals and pharmaceuticals and exports mainly oil, gas, timber and other raw materials. Russia has steadily a positive trade balance.

In December 2011 the Ministry conference of WTO members approved the set of documents for Russia to join the W T O. Russia works closely with OPEC on issues of oil production. Within the CIS there is an organisation of economic collaboration called the Eurasian Economic Union, the members of which are Russia, Belarus, Kazakhstan, Tajikistan and Kyrgyzstan.

investment factors

SPECIAL FEATURES

The most important investment factor is that regional authorities are striving for foreign investments, and in many cases there are favourable economic conditions for investors in regions. Particular measures include special investment agreements, granting local tax concessions for investors and other benefits.

Offshore Facilities

Russian experience in setting up offshore zones (zones of favourable economic environment as they are referred to in the legislation), might not be considered a complete success. The first experiment establishing a zone of favourable economic environment was undertaken in 1994 by setting up an offshore zone in Ingushetia in order to stimulate economic growth and attract investments to the region. However, this measure appeared to be ineffective and the offshore status of Ingushetia was cancelled few years later. At present, similar zones in Russia exist only at regional levels, when regional authorities lower domestic tax rates. However, taking into account the costs of setting up companies and running costs, net savings in using this facility are insignificant. The practice of using such zones is becoming less widespread and it is expected to cease soon.

Agreements on Division of Production

Russian legislation stipulates the possibility of agreements on the division of production, applied for investors mining minerals or natural resources in the Russian Federation. The essence of the agreement is that the investor exchanges its tax liability for an obligation of supplying part of the

production to the state. Agreements on the division of production are applied in the mineral resource, oil, and gas industries. Such agreements imply a special tax regime for the investor. The Tax Code states that an investor involved in an agreement on the division of production has certain tax exemptions for transport tax, property tax, and other local taxes. Depending on the type and content of the agreement on the division of production the investor may be exempt from tax on profit and other taxes.

GOVERNMENT INCENTIVES

For the last few years the government has been aiming at boosting economic activity and attracting investments, including foreign capital, into the Russian economy.

Taxation of foreign companies does not significantly differ from that of Russian entities. However regional or local authorities may grant concessions on certain taxes within their jurisdiction. Each particular matter should be considered independently and concessions are typically available on the basis of significant investment.

SOURCES OF FINANCE

Local sources of finance include Russian banks, subsidiaries of foreign banks, direct investment funds, venture funds and companies providing lease facilities. The government's involvement in financing projects includes shareholdings in natural resources companies, defence industry enterprises and other strategic companies, large banks with state ownership, and state enterprises in different sectors of economy.

One of the features of the Russian financial sector is that equity markets are developing at present and, hence, can hardly be considered as significant source of finance yet.

The main form of financing is borrowing or direct participation in capital including foreign investments. Investors usually require high rates of return, although some large corporations have already obtained credit ratings and their debt is considered as a quite reliable investment. Also, because of the high-inflationary experience of Russia many investors still prefer to denominate credit facilities in foreign currency.

Another feature of debt financing in Russia is the requirement of substantial securities, including pledges of property and guarantees up to the amount of 150% of the sum of credit facilities. This practice is still widespread in Russia though the tendency is declining recently.

FOREIGN EXCHANGE CONTROLS

The primary legislative act on foreign exchange control is the Federal Law "On Currency Regulations and Currency Control". Currency control is provided by the Government, the Central Bank, and authorized banks.

Operations with foreign currency and securities nominated in foreign currency are divided into current currency operations and operations related to the movement of capital.

In a number of cases this division may be relative. Current currency operations and some operations related to the movement of capital are permitted without limitations.

The rest of operations related to movement of capital can be carried out with permission of the Central Bank. Effecting such operations without required permission may cause their invalidation and state confiscation of all the proceeds of the transaction.

The tendency to liberalisation of currency control is being vividly outlined recently. More and more currency operations do not require any permission. Extensive reform of currency control legislation is being debated at government and parliament levels.

EMPLOYMENT REGULATIONS

Currently the principal law applicable to employment regulations is the Russian Labour Code. Key aspects of the labour relations system are described below:

Wages

Monthly wages differ greatly from one region of Russia to another. According to statistical information the monthly average wage varies from approximately 17,000-20,000 RUB (South region, Privolzhskiy region, and Siberia region) to about 40,000-50,000 RUB (North-West region, Central region, Ural region, and Far-East region).

The basic rate of personal income tax is set at 13%. For certain types of income rates of 9%, and 35% are applied. Income of non-residents (expatriates, etc.) is taxed at 30%.

Working Hours

The length of the workweek should not exceed 40 hours per week. The Labour Code provides for shorter working hours under certain conditions: shift work, night work etc.

Limited overtime is permitted for certain workers, not to exceed four hours in two successive days or 120 hours per year. If employees are working a longer week at their own choice, the maximum overtime cannot exceed 4 hours per day and 16 hours per week.

Overtime is payable at higher rates per hour or should be compensated by additional days-off.

For certain employee categories variable working hours may be established. In this case such employees are entitled to at least 3 extra days of vacation.

In general, employees are entitled to paid Russian national holidays and annual leave of not less than 28 calendar days. Employees are able to use their annual leave after six months work.

Labour Contracts and Collective Agreements

The labour contract should be concluded between the employer and the employee either in form of an individual contract or a collective agreement. It determines all the rights and obligations of employees and employer. The Labour Code indicates that the labour contract may contain essential and additional conditions.

The essential conditions include: place of work (structural division), commencement of work, position, qualifications, profession, rights and obligations of the employee and the employer, working conditions, and social insurance.

Additional conditions may include: trial period, confidentiality, obligation to work after education (at the expense of the employer), etc.

Employers are required to conclude an individual written labour contract with each employee (collective labour contracts are also permitted). The duration of the individual labour contract may not exceed 5 years or the contract should be effected as termless (without time-limit). On signing the contract a certificate of acceptance of an employee should be issued by the employer.

Role of Trade Unions

Trade unions are empowered to control the observance of the labour law. According to the Labour Code, the views expressed by trade unions should be

considered by employers in decision making. Decision taken without consensus with trade unions may be appealed to the courts.

Social Insurance and Pension System

State policy in medical insurance, social support and the pension system is implemented via special state funds: the Pension Fund, the Social Insurance Fund, and the Medical Insurance Fund. Having a branch network all over the country the Funds accumulate financial resources for social payments, pensions and medical services.

The legislation sets out following types of pension:

- old age pension;
- disability pension;
- pension for long service;
- social pension.

The old age pension is fixed for males at the age of 60 and for females at the age of 55.

Pension reform being implemented in Russia now aims at a transition from an unfunded pension scheme to a mixed one, with elements of accumulative pension schemes.

Accordingly, the old age pension is divided into three components:

- *the base component*, the amount of which does not depend on the seniority and sum of allocations to the Pension Fund. This component provides the minimum social insurance arrangements.
- *the insurance component* is financed by current payments to the Pension Fund pro rata to seniority and personal allocations to the Fund.
- *the accumulative component* is financed by the corresponding share of allocations to the Pension Fund and investment income thereon.

Major resources for the Pension Fund are generated from social insurance contributions (the former – the unified social tax) paid by employers. Social insurance contributions are to be paid at rates fixed by the law. The tax base for the social insurance contributions is the payroll. Tax rates are regressive and depend upon the type of business (e.g. agricultural firms may pay tax at a lower rate)

Status of foreigners

There are quotas for foreign employees in Russia to support the principles of priority for Russian internal labour resources. These quotas are set out by the Russian Government annually in accordance with the demographic situation in particular regions of Russia.

To obtain the right to hire a foreigner it is necessary to get permission from the local department of the Ministry of Internal Affairs by presenting the decision of the local department of the Ministry of Labour confirming the expediency of employing foreign labour.

Each employee or prospective employee must receive a work permit from the Migration Authorities before being allowed to work in the Russian Federation.

types of business organisations

PRINCIPAL FORMS OF BUSINESS

Russian legislation provides for different types of legal entities.

Legal entities are divided into commercial and non-commercial organisations (companies, partnerships, producers' co-operatives, and state and municipal enterprises).

Companies may be formed as joint-stock companies, limited liability companies, and additional liability companies. Partnerships are divided into general partnership (or full partnership) and limited partnership (partnership on trust).

In addition, a foreign investor may either establish a representative office or branch of a foreign legal entity, or participate in joint activity agreements, also known as simple partnerships.

Joint-stock companies

A joint-stock company (AO) is a company with a charter capital divided into a defined number of shares with a par value. Shareholders are not liable for the company's liabilities but bear the risk of losses arising from the company's activity only for the par value of their shares. There are two types of joint-stock companies:

1) Open joint-stock company (otkrytoe aktsionernoe obschestvo - OAO) is a legal entity, whose shares may be publicly traded without the permission of other shareholders. OAO can distribute its shares to an unlimited number of shareholders and sell them without limitations. The statutory minimum charter capital is 100,000 Russian roubles.

2) Closed joint-stock company (zakrytoe aktsionernoe obschestvo - ZAO) is a legal entity, whose shares are distributed among a limited number of shareholders. The number of shareholders should not exceed 50. The statutory minimum charter capital is 10,000 Russian roubles.

Founders of a joint-stock company sign a written agreement for its formation, under which the procedures necessary for the setting up of the company are carried out, the size of the authorized capital, types and categories of shares to be allocated between founders, amounts to be paid for the shares, the order of settlement of payments, rights and responsibilities of founders in connection with the formation of the company. The constitutive document is the organisation charter, which contains the following information: full and brief names of the company, address of the location of the company's office, company's type (OAO or ZAO); quantity, par value, categories of shares (ordinary, preferred) and types of preferred shares to be allocated; rights of shareholders of each category of shares, the sum of the authorized capital, structure and competence of company's management bodies and boards, and the procedures of the decision-making process, the order of preparation and conducting of a shareholders' general meeting, including a list of issues, which are to be decided upon by a qualified majority or unanimously, information about subsidiaries or representative offices; other information as prescribed in the federal law "On Joint-Stock Companies".

Joint-stock companies are required to register the issue of shares with Federal Financial Markets Service. This is to enable the shares to be traded either publicly (for OAO) or among a limited number of persons (for ZAO).

For registration a set of documents should be submitted to the Federal Financial Markets Service. The procedure usually requires 30 days from the moment of receipt of documents by the registration agency.

Limited liability companies

Limited liability company (obschestvo s ogranichennoj otvetstvennostju – OOO) is an entity with capital stock divided into “parts” (in Russian – dolia), the size of which are determined by the formation documents. Dolia is not a security and it is outside the scope of the Russian securities’ law. An owner of the dolia is not called a shareholder, but a “participant” of the OOO. The company’s capital is formed by the contributions of the participants. The number of participants may not be more than 50. The statutory minimum charter capital is 10,000 Russian roubles. An OOO may not have another commercial organisation consisting of one participant as its only participant. Participants in a limited liability company are not responsible for the company’s liabilities and are responsible for losses only up to the value of their parts.

The founders of an OOO sign the formation agreement and ratify the organisation charter of the company. The organisational charter is the formation document of the company.

The most popular forms of business organisation are OOO and ZAO.

Additional liability companies

Additional liability company (obschestvo s dopolnitelnoj otvetstvennostju – ODO) - a company established by one or more founders, the capital stock of which is divided into parts of sizes determined in the constitutive documents. Participants of such companies are jointly liable for the company’s liabilities in the amounts proportionate to their individual contributions. The vicarious responsibility

of the participants distinguishes an ODO from OAO, ZAO, and OOO. This form of company is very rare in Russia.

General partnerships

General partnership (polnoe tovarischestvo – PT) is a commercial organisation, the members of which (partners) in accordance with the written partnership agreement carry out business activities on behalf of the partnership and have personal responsibility for its liabilities. General partnerships operate under constitutive agreements, which are signed by all members of the partnership.

Limited partnerships

Limited partnership (tovarischestvo na vere – TV) is a commercial organisation in which there are partners and limited partners. Limited partners are investors who bear the risk of losses up to the amount of their investments and do not participate in the business activities of the partnership.

Partnerships are generally not very popular in Russia and are usually used only for conducting a limited set of activities such as legal services, audit assurance, etc.

Branches and representative offices

A representative office is a subdivision of a legal entity located at a place other than the head office of the legal entity, which represents the interests of a legal entity. A branch is a subdivision of a legal entity located at a place other than the head office of the legal entity, which performs all or part of the legal entity’s functions, including representation.

Both representative offices and branches share the following attributes:

- They are established as subdivisions; they do not enjoy the rights of a legal entity and operate on the basis of Regulations;

- They are located away from their parent legal entity;
- They are allotted property by the legal entity;
- They act on behalf of the legal entity;
- Heads of branches and representative offices are appointed by the parent legal entity and act on the basis of an issued Power of attorney;
- Responsibility for the actions of branches and representative offices remains with the foreign (parent) legal entity.

The distinctions between representative offices and branches are as follows:

- Branches have a wider scope of powers than representative offices: apart from representing interests, branches can be engaged in production and business operations; representative offices normally limit their activities to non-commercial functions, such as marketing or information gathering;
- Branches are accredited for a longer period than representative offices.

Joint activity agreements

A joint activity agreement is not a legal entity but represents the pooling of assets for the common conduct of business. One of the parties of any joint activity agreement must be a Russian legal entity.

FORMAL STATE REGISTRATION OF COMMERCIAL ORGANISATIONS

State registration of commercial organisations is conducted by the Federal Tax Service of the Russian Federation.

For the purpose of state registration a company must submit the following documents:

- the standard form application for state registration, signed by the applicant (his/ her signature has to be notarised);
- decision to form the legal entity in the form of record, agreement or other

document prescribed by legislation of the Russian Federation (mainly the protocol of the founders' meeting or the resolution of the sole founder on the establishment of the company);

- the charter of the company;
- extract from the state or trade register of foreign legal entities of the country of origin or other evidence of the legal status of a foreign founder (participant) if any;
- confirmation of payment of the state registration fee.

State registration is due within five working days from the date of submitting the whole set of documents to the registration body.

Companies (mostly OOO) can be bought off the shelf from specialised commercial organisations. This practice is not widespread for foreign investors, as the latter prefer the formation of a new entity. Recently registering and keeping ZAO and OAO available for sale has become rare among companies specialised in companies' registration services as the formation of ZAO and OAO needs more costly procedures, which should be personalised, and therefore are not always convenient for keeping them on the shelf.

The professional fees for company formation depends very much on the type of entity, place of registration and timing requirements. Thus the fees should be agreed on individual basis.

LEGAL, ACCOUNTING, AND AUDIT REQUIREMENTS

With the developing legal system in Russia some important changes in regulation of the business have taken place. Major requirements concerning legal, accounting, and audit matters are described below.

Legal Requirements

All companies and individual entrepreneurs are subject to state and tax registration. The registrar is the Federal Tax Service of the Russian Federation.

The registering information is open to the public with some exceptions having limited access.

Besides legal registration, all companies and individual entrepreneurs have to be registered as tax payers in the local Tax Office where they reside, have branches, immovable property or/and vehicles. Registration with Statistics Authorities and social security funds is also required.

Accounting Requirements

All companies in Russia are required to keep accounting records in order to provide complete and reliable information on business activity for external and internal users. There are some alternative accounting requirements for small companies. Small companies may have simplified accounting records and present simplified accounts. The general balance sheet date is 31 December.

Current accounting regulations are based on the Law "On Accounting" of December 1996, Russian Accounting Standards and various regulations from the Ministry of Finance. A new Federal law "On Accounting" of December 2011 enters into force from January 1, 2013. The legislation requires all companies to present annual and interim (quarterly) financial reports. All companies present financial reports to their shareholders/owners and to local statistic bodies and to tax authorities.

In addition, from January 1, 2012 the Federal Law "On consolidated financial statements" requires preparation of consolidated financial statements by group holding companies.

The programme for reforming Russian accounting procedures in accordance with International Accounting Standards established and being implemented by the Russian Government aims at the harmonization of accounting principles applied in Russian accounting with Generally Accepted Accounting Principles.

Audit Requirements

In accordance with Russian auditing legislation, some companies are obliged to have their annual statutory financial statements audited.

- Compulsory audit is stipulated for the following non-governmental organisations:
- all open joint-stock companies (OAO);
- banks and other credit institutions, insurance companies, commodity and stock exchanges, investment funds, charitable and other (non-investment) funds, etc.;
- other companies with either annual sales exceeding 400 million roubles for the reporting year or total balance sheet assets exceeding 60 million roubles for the reporting year;
- state and municipal unitary enterprises and companies where the state owns more than 25%.

taxation

FISCAL YEAR

The fiscal year in Russia is the calendar year. Companies are not allowed to change their fiscal year-ends (Companies cannot change their own financial year-end or use that of their foreign parent company). Shorter tax periods may be prescribed for certain taxes.

General Structure of Taxation

The Russian tax system consists of federal, regional and local taxes.

Federal taxes are:

- corporate profits tax;
- value-added tax;
- customs duties;
- excise duties;
- personal income taxes;
- other federal taxes;
- as well as social insurance contributions.

Regional taxes are:

- corporate property tax;
- transport tax;
- other regional taxes.

Local taxes are:

- land tax;
- individual property tax.

Federal taxes are levied throughout the territory of the Russian Federation, while regional and local taxes are levied on the taxpayers registered, operating or holding property within the territory of the region (municipal district).

Federal tax rates are set by the Tax Code at federal level. Regional and local authorities however may reduce the regional and local part of the corporate profit tax rate respectively within the limits prescribed by the Tax Code.

The rates of regional/local taxes are normally set and respective concessions are granted at the regional/local level (within the limits set out at federal level). The results vary over the territories: some introduce as many taxes as possible and raise their rates to the maximum; others refrain from introduction of excessive number of taxes and use their authority to establish lower tax rates, thus, offering a more favourable tax regime as a lure for investments.

CORPORATE PROFITS TAX

Corporate profits tax is payable in Russia on the profits of Russian legal entities and foreign legal entities carrying out business activities in the Russian Federation, calculated as operational and non-operational income less tax deductible expenses and losses.

It is still possible for profits taxation purpose to recognise revenue either on a cash or on an accruals basis. However, the choice of cash method is not available to taxpayers with average quarterly income exceeding 1 million roubles (excluding VAT and sales tax).

Under the accruals basis operational income and expenses are recognised when they are accrued, while under the cash method they are recognised when paid.

From January 1, 2002 a corporate taxpayer must maintain a tax accounting system for purposes of calculating corporate profits tax (CPT) liabilities. Reconciliation between accounting and taxable profits is required.

Deductibility of certain categories of business expenses and losses is restricted under the Russian taxation rules, while a few types of expenses are non-deductible at all.

The general profit tax rate is set at 20 per cent of the taxable business profits, where 2 per cent is payable to the federal treasury, and 18 per cent to regional treasuries. Additionally, the regions have been granted the power to decrease the regional rate down to 13.5 per cent for certain categories of taxpayers.

Enterprises and organisations, that are legal entities created under Russian Law, are subject to the corporate profits tax (CPT) with certain exceptions:

- entities subject to unified tax on imputed income;
- small enterprises using simplified tax and accounting systems;
- gambling businesses (this income is subject to a special tax on gambling businesses);
- agricultural entities (with the exception of agricultural enterprises of an industrial type).

The tax period is a calendar year. The reporting period may vary, depending on the CPT payment system, used by a taxpayer:

- if a taxpayer uses a quarterly system, the reporting periods are first quarter, half year, and 9 months of the year;
- if a taxpayer makes monthly advance payment of CPT based on actual profits, the reporting period is a month, two months, three months and so forth till the end of the calendar year.

Taxable income consists of sales income and non-operational income. Income in tax accounting is classified as follows:

- income from sales of goods (works, services);
- income from sales of purchased goods (merchandise inventory);
- income from sales of fixed assets;
- non-operational income.

The Tax Code provides for special tax rates on dividends receipts and distributions.

If an entity receives dividends it pays CPT at:

- 9% if dividends are received from a Russian legal entity;
- 15% if dividends are received from a foreign legal entity.

When making a calculation of the dividends amount subject to withholding tax, the tax agent takes all dividends subject to distribution and deducts the amount of dividends received by the tax agent itself in the reporting period. The remaining portion is subject to withholding tax.

Under the laws of the Russian Federation, a representative office/branch of a foreign company is not a Russian legal entity. A foreign company will not be subject to Russian tax on its net business income unless its Russian presence sets up a permanent establishment.

For Russian taxation purposes, a foreign legal entity has a permanent establishment when it conducts certain business activities in Russia through a representative office or other permanent place used for the regular conduct of such business activities. A permanent establishment is defined in the Tax Code as "a branch, division, office, bureau, agency, or any other place through which a foreign legal entity regularly carries out its business activities in Russia."

The profits derived through a permanent establishment are taxed in Russia at the common CPT rate.

Withholding tax rates where a foreign legal entity does not create a permanent establishment in Russia and is not protected by a double taxation treaty are described below:

- 10% on income from use or lease of transportation vehicles used in international traffic;
- 15% on dividends received from Russian legal residents;
- 20% for capital gains on immovable property when net book value or acquisition cost can be deducted from gross revenue or 20% on gross amount of revenue from disposal of immovable property (without deduction of costs);
- 20% for capital gains arisen from disposal of shares of Russian companies, more than 50 % of whose assets consists of immovable property situated in Russia;
- 20% on other types of income.

PERSONAL INCOME TAX

Personal income tax (PIT) is the tax levied on physical persons. Whether a particular individual is liable to the tax or not depends on that person's:

- residence; and
- type of income.

According to the Tax Code a tax resident is a person who stays in the Russian Federation for not less than 183 days in a calendar year.

Taxation of residents and non-residents is different:

- residents are taxed on their world-wide income;
- non-residents are taxed on income from Russian sources.

The tax period for PIT purposes is a calendar year.

The standard tax rate is 13 % (flat).

An increased rate of 35% applies to the following income:

- taxable portion of prizes and awards received at competitions and/or games conducted for advertising purposes;
- taxable insurance payments under life insurance agreements concluded for less than five years;
- interest on bank deposits not exceeding Central Bank rate on rouble deposits and 9% on deposits in foreign currency;
- benefit received in the form of low (zero) interest on corporate (non-bank) loans (imputed interest income);

An increased rate of 30% applies to all types of income received by non-tax residents of Russian Federation.

A rate of 9% applies to dividends received by Russian tax residents.

Some types of income may be fully or partially exempt from taxation if certain conditions are met.

The major exemptions and related conditions are as follows:

- government support payments, excluding sick leave payment;
- state pensions;
- payments to individuals of compensatory nature and business expense reimbursements;
- alimonies;
- scientific, cultural, educational grants from foreign organisations;
- one-off financial aid;
- payments made by employers to Russian recreation and resort facilities for the benefit of employees;
- medical treatment payments made by employers for the benefit of their employees;
- scholarships;
- others.

The following business travel expenses reimbursed to employee are not subject to personal income tax:

- per diem allowance (within statutory norms);
- travel costs (including taxi to and from airport);
- airport fees and commission charges;
- luggage fare;
- accommodation expenses (hotel);
- business communication expenses.

All costs (except per diem allowances) must be supported by appropriate documents. In the absence of such documents the amounts will be fully taxable with the exception of accommodation expenses which will be taxable on any amounts that exceed statutory limits.

VALUE-ADDED TAX

Value added tax (VAT) is generally chargeable on the sale of all goods and services in Russia and on the importation of goods into the territory of the Russian Federation. The standard rate of VAT is 18% from January 1, 2004. Certain food products and goods for children are charged a 10% VAT, while exports of goods and related services are subject to VAT at 0% rate.

Sales of certain goods (works, services) are VAT exempt. VAT rules for exempt operations and those subject to 0% rate are very different.

Input VAT (i.e. VAT paid to suppliers) is generally allowed as a credit against output VAT (i.e. VAT charged to customers and payable to the budget) after services/materials/fixed or intangible assets are paid for and reflected on the books.

Exemption from VAT of certain sales may be disadvantageous to the supplier since VAT incurred on inputs may not be recovered, but should be instead charged to the costs of production.

Sales subject to 0% VAT (e.g. exports) allow recovery of input VAT.

There is a uniform invoicing procedure for VAT purposes applicable to all taxpayers providing goods, works, or services. VAT invoices of a standard format (“schet-factura”) are to be issued and registered in a sales journal of the seller and incoming VAT invoices from suppliers are to be recorded in a purchases journal of the buyer. Compliance with these invoicing procedures is critical to the buyer’s ability to recover VAT.

Supplies on which VAT is chargeable may be made by entities which have no presence or tax registration in Russia (e.g. foreign entities). In this situation, the recipient of the service (as described in the Tax Code – a tax agent) must withhold VAT from the payment to the supplier, at the same time this VAT may be credited by the tax agent as input tax, provided certain requirements are met.

SOCIAL INSURANCE CONTRIBUTIONS

There are two principal groups of social insurance contributions payers:

- employers, including organisations, individual entrepreneurs (on payments to employees);
- individual entrepreneurs (on their business income).

Social insurance contributions include contributions to statutory pension, medical and social insurance funds.

Social insurance contributions are calculated for each employee individually on a regressive basis as shown in table below:

Tax base per employee	Tax rate
Up to RUB 512,000	30%
Over RUB 512,000	10%

CORPORATE PROPERTY TAX

Corporate property tax is a regional tax. It may be set by regional authorities in line with federal legislation outlining the general principles for applying this tax.

Corporate property tax is payable by:

- enterprises, organisations with a status of legal entity;
- foreign legal entities, having taxable property in Russia.

Individual entrepreneurs and physical persons are not subject to corporate property tax.

From January 1, 2004 the average value of property comprising fixed assets (movable and immovable) less accumulated depreciation is subject to corporate property tax at the rate of 2.2%. The tax rate is subject to lowering by regional authorities.

IMPORT TARIFFS (CUSTOMS DUTIES)

The majority of customs duties in Russia are “ad valorem”. There are also specific duties for certain types of imported goods, which are based on the volume, weight or quantity of imported goods. Some duties have a combined rate mixing the above two types of duty rates and, therefore, the tax basis may differ. Base duty rates vary widely, from 100% on spirits to 0% for printed matter, some food products and some other imports.

TRANSPORT TAX

From January 1, 2003, the regional authorities have the ability to set a transport tax. The tax is based on the engine capacity of a vehicle. The exact tax rate is established by the regional authorities within the allowed limit.

STAMP DUTY

Stamp duty is obligatory throughout the entire territory of the Russian Federation. It is paid on executing legal contracts or issuing documents by authorized bodies or functionaries in the Russian Federation.

Payers of stamp duty are citizens of the Russian Federation, foreign citizens, and legal entities, which apply for documentation or executing legal actions.

Stamp duty is paid:

- on suits or complaints brought to courts of general jurisdictions, arbitration courts, and the Constitutional Court of the Russian Federation
- on execution of notarial deeds by notary officers of state notary's offices or authorized functionaries of executive authority bodies, local authorities and consular offices of the Russian Federation;
- on state registration of acts of civil status and other legal actions, executed by civil status registering bodies;
- on state registration of legal entities, including state registration of changes and additions to the constitutive documentation of legal entities;
- on issuing documents by certain courts, bodies, and institutions;
- on issuing documentation related to the acquisition of or giving up of citizenship of the Russian Federation.

TAX TREATIES

Russia is a successor state of the former USSR as a party to tax treaties, which may provide relief in the form of reduced or zero rate of withholding tax. At the moment Russia has tax treaties for the avoidance of double taxation with the following countries:

TAX TREATIES	DIVIDENDS %	INTEREST %	ROYALTIES %
Armenia	5/10	0	0
Austria	0	0	0
Azerbaijan	10	0/10	10
Belgium	10	0/10	0
Belarus	15	10	10
Bulgaria	15	15	15
Canada	10/15	0/10	0/10
China	10	0/10	10
Croatia	5/10	10	10
Cyprus	5/10	0	0
Czech Republic	10	0	10
Denmark	10	0	0
Egypt	10	15	15
Finland	0	0	0
France	5/10/15	0	0
Germany	5/15	0	0
Hungary	10	0	0
India	10	0/10	10
Ireland	10	0	0
Israel	10	10	10
Italy	5/10	10	0
Japan	15	0/10	0/10
Kazakhstan	10	10	10
Kyrgyz Republic	10	0/10	10
Lebanon	10	5	5
Luxemburg	10/15	0	0
Macedonia	10	10	10
Malaysia	15	15	10/15
Mali	10/15	0/15	0
Morocco	5/10	10	10
Moldova	10	0	10

Mongolia	10	10	20
Namibia	5/10	10	5
The Netherlands	5/15	0	0
North Korea	10	0	0
Norway	15	0	0
Poland	10	10	10
Philippines	15	15	15
Qatar	5	5	0
Romania	15	15	10
Serbia and Montenegro (formerly Yugoslavia)	5/15	10	10
Slovak Republic	10	0	10
Slovenia	10	10	10
South Africa	10/15	10	0
South Korea	5/10	0	5
Spain	5/10/15	0/5	5
Sweden	5/15	0	0
Switzerland	5/15	0/5/10	0
Turkey	10	10	10
Turkmenistan	10	5	5
Ukraine	5/15	10	10
United Kingdom	10	0	0
USA	5/10	0	0
Uzbekistan	10	10	0
Vietnam	10/15	10	15

HLB in Russia

how to contact us

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