



RUSSIA: THE BEAR ESSENTIALS

ALEXANDRA KADET OF PRICEWATERHOUSECOOPERS REVIEWS THE ESSENTIALS FOR TREASURERS WHOSE COMPANIES ARE PLANNING TO DO BUSINESS IN THE RUSSIAN FEDERATION.

Today we can talk about the Russian Federation as a state that welcomes foreign investment and activity. For the past 12 years, the Russian government has done a lot of work in the field of legislation. However, the regulatory environment might still be considered to lag somewhat behind the highest standards found globally.

So what is it like running a business in Russia nowadays? This article contains a brief overview of the Russian business environment and looks at some of the latest changes in legislation. While it is, of course, not possible to discuss all the issues in great detail here, I shall try to summarise clearly some of the key aspects to be considered when structuring business operations in Russia.

GETTING STARTED. A key issue when commencing business activity in Russia (as in any other country) is selecting the type of presence which is most suitable for your company. In terms of the legal forms of organisation to be adopted, there is a variety of options. The main structures are set out in *Table 1*.

If maintaining activity in Russia without any formal presence, one should consider the risk of 'permanent establishment' in Russia for tax purposes (see also *The Treasurer's Handbook 2003*, p52-57). The new tax code contains a number of activities that, when conducted by a foreign legal entity, result in a permanent establishment or taxable presence in the Russian Federation. There are also a number of business activities which require specific business licensing, for example, insurance, banking, credit and pharmaceutical activity.

REGISTERING WITH TAX AUTHORITIES. Where a foreign legal entity – its branch or representative office (RO) – conducts, or intends to conduct, activities in the Russian Federation for a period exceeding 30 calendar days in a year, it has to register with the local tax authorities (at its place of business) no later than 30 days after the commencement of the relevant activity.

The registration of those conducting activities in the Russian Federation, within a period not exceeding 30 calendar days in a year, is put in place by forwarding notices in a specific form to both the tax authority responsible for registration of foreign legal entities at their place of business and to the Ministry of Taxation of the Russian Federation. The notice shall be forwarded prior to the commencement of activity in Russia.

Foreign legal entities are required to register with the tax authorities, irrespective of whether any tax liability arises to the company under Russian legislation. Among the documents that must be submitted for registration purposes are: an application for registration in a specific form; abstract from the commercial register or the certificate of incorporation (or another similar document containing information on the legal or juridical person that has registered the foreign legal entity), the registration number, date and place of registration.

OPENING A BANK ACCOUNT. Non-resident companies can open bank accounts of types K (convertible account), N (non-convertible account), or F (individual account) with authorised banks. A bank account agreement may be concluded in the name of the foreign company by the head of a branch (or RO) of the company, operating

under a power of attorney issued by the non-resident firm.

To open a bank account, a non-resident entity (other than a foreign bank) must present documents to an authorised bank, as required under Russian legislation. These include documents confirming the company's legal status under the law of the country where the legal entity has been established (in particular, the company's charter and documents confirming the legal entity's state registration),^â and a copy of the regulations of the branch (or RO) accompanied by a Board minute, or similar, confirming the decision to establish the branch (or RO).

FUNDING ACTIVITIES IN RUSSIA. In recent years, developments have tended towards liberalisation. This is clearly seen in the field of banking, currency legislation and foreign exchange (FX) regulations. Forecasts for the financial sector in Russia are generally positive. As a result, it is now easier to obtain local bank funding, especially for more creditworthy business, but spreads are still expensive. The central bank refinancing rate is 16%. However, many foreign-owned businesses in Russia continue to seek group funding or funding from banks outside Russia. However, thin capitalisation rules do apply in Russia to funding by an overseas parent.

In summary, where a taxpaying Russian legal entity has a debt financing from a foreign legal entity, which directly or indirectly has under its ownership more than 20% of the authorised capital of the Russian company, and the outstanding balance of the loan exceeds equity capital by more than three times, interest is not deductible for tax purposes and payments of interest will be treated as distributions.

■ TABLE 1
MAJOR AVAILABLE STRUCTURES

	REPRESENTATIVE OFFICE (RO)	BRANCH	A/O AFFILIATE OR ASSOCIATED COMPANY (MORE THAN 20% OWNED BY A FOREIGN LEGAL ENTITY)
LEGAL FORM	Not a separate legal entity Must be registered in the State Committee of Statistics and accredited in the State Registration Chamber.	Not a separate legal entity	Legal entity, must be registered in the Ministry of Taxation of the Russian Federation* and the State Committee of Statistics.
TAX REQUIREMENTS	There is no difference between RO and Branch for tax purposes. Both of them must pay profits tax (24%) in case of taxable activity and other taxes		Similar to the Russian legal entities: profits tax (24%) and other taxes depending on the activity
LOCAL REPORTING	Reporting to tax authorities once a year if no commercial activity is maintained, in other case similar to the branch In all cases it is obligatory to report to the Social Security Funds	Monthly, quarterly and annual reporting, depending on activity and taxes paid	Monthly, quarterly and annual tax reporting
AUDIT REQUIREMENTS	Not obligatory	Not obligatory	Obligatory auditing*** for companies where sales revenue for one year is 500k times more than the minimum earnings (100 roubles ≈ \$3.30)
PERMITTED ACTIVITIES	<i>De jure</i> is not permitted to maintain any commercial activity. <i>De facto</i> if tax registered there have been no cases when RO had any problems.**	The same as ordinary legal entity	All kinds

* The Ministry of Russian Federation for Taxes and Levies is authorised to run the state registration of all legal entities in Russia. ** There are different wordings in civil and tax legislation.
*** Auditing is also obligatory for credit institutions, insurance companies, investment funds, etc.

CURRENCY CONTROLS. There are fairly strict requirements concerning currency regulation. ROs and branches should not have any problems about obtaining foreign currency from their head office or distributing profits abroad. Equally, there are no obstacles for a Russian joint stock company paying out dividends to an overseas shareholder. In other cases, when a legal entity in Russia wants to transfer funds abroad in the currency other than Russian roubles, there are different procedures that sometimes require licensing. The application of currency regulation should be carefully considered in each particular situation and appropriate advice taken.

Although Russian legal entities are now permitted to open accounts with foreign banks, the transactions that can be executed on these accounts are limited. It is useful to know that sometimes a foreign legal entity will not need an account with a Russian bank to pay taxes. For example, when owning a property in Russia, an overseas company pays property tax, but can do so from any of its accounts abroad.

LOOKING AHEAD. For many years, companies have been reluctant to do business in Russia. The unstable and arguably weak economic situation, corruption and the like, made the investment climate very unattractive. Now the sphere of investment and business incubation is under the influence of a far more stable economic climate. Since Russia was taken off the Financial Action Task Force (FATF) blacklist, it was a sign that it was on its way to international standards of business conduct. Major consulting firms now have a wide network of clients in the region, which is also an indication that companies both inside and outside the country are operating actively in the Russian market.

Although the Russian legislative environment is still quite complex and unfamiliar, from the international point of view, there remain real opportunities to plan a profitable business in the region.

Alexandra Kadet is Tax Associate at PricewaterhouseCoopers.
alexandra.kadet@ru.pwc.com
www.pwcglobal.com

BOX 1
USEFUL RESOURCES

With English language option on main web page:
 The Central Bank of Russia www.cbr.ru
 Ministry of the Russian Federation on Taxes www.nalog.ru
 Russian legislation www.garant.ru
 Russian economy (links) www.russianeconomy.org/links.html
 PricewaterhouseCoopers www.pwcglobal.com/ru/eng/main/home/index.html

Site in Russian language with no English option on main web page:
 Vedomosty (newspaper) www.vedomosti.ru
 Government of RF www.government.ru

English websites
 Expert (magazine) <http://eng.expert.ru/expert/>
 State Committee on Statistics <http://www.gks.ru/eng/>

JSC OR LLC (NOT ASSOCIATED, IE LESS THAN 20% OWNED BY A FOREIGN LEGAL ENTITY)	JOINT VENTURE	
	PURE JV	PARTNERSHIP
Legal entity, must be registered in the Ministry of Taxation of the Russian Federation* and the State Committee of Statistics.	This particular partnership is not a legal entity, but is transparent for tax purposes. Partners (only legal entities or) pool their contributions and act jointly without forming a legal entity to gain profit. The assets contributed by partners shall be recognised as their common property. NB: Many specific issues to be considered	Legal entity. must be registered the Ministry of Taxation of the Russian Federation* and the State Committee of Statistics.
Similar to the Russian legal entities: profits tax (24%) and other taxes depending on the activity	Partners pay profits tax according to their share of profits. Other taxes can be paid by one of partners if agreed.	Similar to the Russian legal entities: profits tax (24%) and other taxes depending on the activity
Monthly, quarterly and annual tax reporting	Monthly, quarterly and annual tax reporting	Monthly, quarterly and annual tax reporting. It is obligatory to report to the Social Security Funds
Obligatory auditing*** for open joint-stock companies and for companies where sales revenue for one year is 500k times more than the minimum earnings (100 roubles ≈ \$3.30)	Not obligatory	Obligatory auditing*** for companies where sales revenue for one year is 500k times more than the minimum earnings (100 roubles ≈ \$3.30)
All kinds	All kinds	All kinds