

Changes regarding personal income tax to be introduced to the Tax Code

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The recently adopted and published federal law of 19 July 2009 No. 202-FZ introduces significant changes to Chapters 23 and 25 of the Tax Code regulating personal income tax and profits tax matters. These changes will come into force from 1 January 2010.

Below we provide a brief overview of the changes relating to personal income tax.

Non-taxable income

The list of instances where material gain received by the taxpayer is not subject to income tax would be expanded to include the following:

- Material gain resulting from low interest or interest-free loans for the purchase of plots of land where residential real estate is located or would be constructed
- Material gain resulting from low interest or interest-free loans used to refinance previously extended loans for the purchase of residential real estate or plots of land where such property is situated or would be constructed.

Further, income from the sale of a car which was owned by an individual for more than three years would be non-taxable. This change practically leads to the avoidance of the administrative burden of filing of tax returns with sole aim to report such income even though the car was sold at a loss.

Social tax deductions

At the moment individuals can apply for social tax deductions in respect of contributions paid under non-state pension agreements or voluntary pension insurance agreements only on the basis of tax returns filed after the end of a calendar year.

From 1 January 2010 it would be possible to apply for such deductions before the end of the tax year and without submission of a tax return. According to the changes, individuals would be able to request this deduction from their employers.

The new provisions concerning the social tax deductions would apply to contributions made starting from 1 January 2009. Employer will need to establish appropriate internal processes into their payroll systems to manage this new responsibility.

Property-related tax deductions

From 1 January 2010 the taxpayer would be entitled to the following new property-related tax deductions:

1. Deduction in the amount of interest on loans used for the acquisition of a plot of land where residential real estate is located or would be constructed
2. Deduction in the amount of interest on the refinancing of loans used for the new construction, or acquisition, of a house, an apartment, a room, or a plot of land where residential real estate is located or would be constructed
3. Deduction in the amount of expenses incurred in connection with the preparation of design for residential real estate finishing work.

In addition, the limit on the deduction against the proceeds from the sale of property other than real estate which was owned by an individual for fewer than three years would be increased to RUB 250,000 (currently this limit is RUB 125,000).

Credit organizations acting as tax agents

Some changes concern tax agents which are credit organizations. From 1 January 2010 the reporting and withholding procedures for credit organizations in respect of any taxable material gain on loans received by their clients would be changed, and in most cases banks would not be required to withhold tax on this type of income.