

B2B: New Fiscal Law to Increase the Property Tax Burden on Individuals

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At the beginning of October, a long-anticipated new law was enacted, amending the Russian Tax Code in terms of property tax on individuals (Federal Law No. 284-FZ dated 04 October 2014 On Amending Articles 12 and 85 of Part 1, and Part 2 of the Russian Tax Code and on Repealing the Law of the Russian Federation On property taxes for individuals (the Law).The law is one of the major steps in the Russian Government's real estate taxation reform plan, but its entry into force has been delayed until Jan. 1, 2015.

As previously announced, the major change lies in the way the tax base is determined for fiscal purposes. For a considerable time, the approach of the Russian authorities was to determine the amount payable by a taxpayer based on the so-called inventory value of the real estate facility in question. In many cases, this differed substantially from the actual market value of the property, meaning that the amount of property tax payable was often quite modest and did not create any significant tax burden for individuals.

Under the new approach set out in the Law, the aim is to calculate tax based on a value of property, which is as close as possible to its real market value. As it obviously would not be practical to establish the real market value for every real estate facility, the Law has determined that the so-called cadastral value of the property should serve as the basis for calculating property tax for individuals. This global assessment procedure is being undertaken at the instruction of local authorities throughout the country. When the cadastral value is assessed in this manner, there may still be differences from the real actual value of individual properties; with a mass assessment, it could hardly be otherwise, but in general, the values will be closer to market value than at present.

The taxable items include an extended list of types of residential real estate, covering residential houses, apartments, a room that is a separate unit within residential premises, garage and parking places, integrated real estate complexes, unfinished construction

facilities, as well as other buildings and constructions owned by individuals.

The Law defines the maximum level of tax rates (this may be up to 2 percent of the cadastral value of the property in question). However, determining the exact rates will be left to legislative bodies of municipal authorities throughout Russia (with Moscow, St. Petersburg and Sevastopol establishing their own rates). The rates and procedures are to be established on the local level by Jan. 1, 2020, with Moscow to approve its own rates by the end of this year (The Moscow City Duma passed the law in question in the first hearing on Oct. 22, 2014.)

Importantly, the Law states that a special approach must be followed to assessing the taxation base in respect of certain types of real estate property. For example, when assessing the tax base with respect to an apartment, the cadastral value of 20 sq.m. should be disregarded. The same approach will apply to a room that is a separate unit within residential premises (10 sq.m. to be disregarded), to a residential house (50 sq.m.), and other types of property. The Law empowers other local legislative bodies to increase the above level of deductions at their discretion.

The Law also gives local authorities the right to establish differentiated tax rates depending on various criteria, including the cadastral value of the real property in question, the type of item being taxed, and where it is located. Needless to say, the Law grants tax reliefs to certain special categories of taxpayer. The taxpayers with such status include persons with disabilities, military personnel, retired persons, etc. A person falling within this criteria may enjoy this tax benefit for one item only of each type of property.

Predicting the actual consequences of the changes in the Law is far from easy. However, it is apparent that individuals will face an increased tax burden as a result of the change in the way the tax base is assessed. This will be especially true for high-value property, and this will have a major impact on the real estate market in Moscow and St. Petersburg in particular.

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