



PERMANENT ESTABLISHMENT IN RUSSIA: BRANCH OR SUBSIDIARY?

DEFINITION OF A PERMANENT ESTABLISHMENT

A 'permanent establishment' (PE) is not an organizational form of business structure, but rather a taxable status of a foreign business operation in another country, in this case in Russia. The term is defined in the Russian Tax Code (art. 306) and in many double taxation treaties. A business may be considered as a permanent establishment when activities in Russia are carried out by a foreign firm through any fixed place of doing business: the office, branch, headquarters, business partner or agent of a foreign company.

The concept of a permanent establishment is often confused with the concept of representative Office (RO), as the Russian terms for them are very similar. Representative office in Russian is 'predstavitelstvo' and permanent establishment is 'postoyannoye predstavitelstvo'. However, the existence of a RO does not determine if the business is taxable or not.

DEFINITION AND MAIN DIFFERENCES BETWEEN A BRANCH AND A SUBSIDIARY

Russian Legal Entity (Subsidiary) – A separate legal entity, registered under Russian law, that bears its own liabilities.

Branch/Rep Office (B/R O) – An extension of the a foreign legal entity accredited to do carry out activities in Russia. Liability is borne by the Head Office or Parent company.

Representative and Branch Offices are not independent legal entities, but rather "sub-divisions" of a parent company. A Rep Office should not engage in commercial activity, but a Branch may.

TAX AND ACCOUNTING OBLIGATIONS

In general the accounting requirements are bit more burdensome for a Russian Legal Entity as quarterly financial statements must be prepared as well as full tax accounting, including VAT.

B/ROs are allowed to file and pay quarterly profit taxes. This is an opportunity for tax planning. No value added tax (VAT) accounting is necessary if there is no commercial activity and VAT is recognized as a cost.

It should be noted that if a BO or RO engages in commercial activity then full tax accounting and reporting is mandatory.

The accounting requirements are not as burdensome – there are no quarterly financial statements, but an annual report on activities (includes quasi-financial statements) is made.

Rep Offices which do not carry out commercial activities are exempt from VAT on their rent payments.



REGISTRATION FORMALITIES

The “accreditation” process, as it is called in Russia, can take much longer for a Rep/Branch office compared to a LLC or JSC, typically 6 to 8 weeks.

In contrast to Russian legal entities, the process of registering a branch or representative office of a foreign company involves several federal and local authorities. To register, branches and representative offices need to take the following steps:

- accreditation with federal bodies. Accreditation is mandatory, since the local banks and administrative authorities may not recognize the branch/representative office without it;
- tax registration;
- registration with state statistic authorities, obtaining statistics codes;
- registration with social (pension, medical and social security) funds;
- opening bank accounts.

For the accreditation of a representative office, accreditation bodies charge a processing fee ranging from USD 2,000, depending on the period of accreditation.

STANDARD LEGAL OBLIGATIONS AND FORMALITIES FOR A BRANCH

There are some advantages of doing business via a Rep/Branch office, such as the ease of moving currency out of Russia and obtaining work visas for staff. However, some activities may be limited or more troublesome such as the import of goods or certain licensed activities.

An accredited representative office is not a Russian legal entity, but an officially recognized subdivision of a foreign legal entity. Although Russian law suggests that the scope of an accredited representative office’s activity would be limited to auxiliary representational functions, in practice many foreign firms conduct commercial activities that, according to a strict interpretation of the law, should only be conducted through a registered branch or a Russian company.