

CONSOLIDATED TAXATION AND ITS CONSEQUENCES FOR REGIONAL BUDGETS

Russia's economic power rests upon large business. Thus, it is essential to develop taxation models for maintaining the balance between the interests of both entrepreneurs and the state, while saving high national budget capacity and business activity. We analyzed a new mechanism of profit taxation regulation for consolidated groups of taxpayers (CGT) in order to assess the impact of CGT on budget revenues formation. Research results have confirmed the hypothesis about low efficiency of tax consolidation. The CGT regime leads to unfair tax revenues distribution among sub-federal budgets, creating budget planning uncertainty. Examples of largest ironworks corporations reveal destructive influence of CGT on regional budget revenues formation: our calculations have illustrated that at least in four Russian regions annual budget losses range from 3 to 9 billion rubles. We have demonstrated the correlation between balanced calculation of tax base within CGT and profit taxation minimization as the main source of corporate owners' growing welfare. Reduced tax burden of consolidated taxpayers is not accompanied by intensified investment activity. We have concluded that consolidation of tax liabilities has led to formally legitimate but unprofitable optimization. A steady decline of tax revenues from consolidated groups has intensified destabilizing processes in regional budget systems and has become a motive for CGT abolition by the government. Considering that consolidated groups formed in the period from 2012 to 2013 will operate until 2023, we propose measures to neutralize the negative consequences of their functioning.

Keywords: consolidated group of taxpayers, tax policy, regional budgets, major taxpayers, ironworks corporations, financial results, tax base, income tax, tax optimization, tax distribution

Introduction

In recent years the Russian economy witnessed an increasing influence of big business, the revenues of which exceed 100 billion rubles. In 2007–2016, their number increased from 36 to 123, and their revenue— from 14 to 52 trillion rubles. It is very important to build optimal relations between the state and big business, because nowadays the largest corporations form half of budget revenues, play a critical role in the competitiveness of the country and determine its place in the global economy.

At the same time, some researchers [1–5] note that the interaction between the state and entrepreneurship, especially major private regional companies, is impeded by certain problems, the origins of which lie in the mismatch between the resource potential of these companies and their real contribution to the territories' development, primarily in terms of budget revenues' sufficiency. This situation is largely determined by the presence of a wide range of tax benefits aimed at stimulating the interests of large business, which not only generates significant budget losses, but also undermines the compliance with the principles of parity and competitive economic development.

Theoretical and methodological framework of the research

Effective interaction between government agencies and large capital depends to a great extent on the nature of tax policy. The tax regime of the groups of companies is determined by general economic policy of the state; and the features of this regime reflect the government's views on stimulating economic concentration and consolidation of business [6].

In world practice, consolidated taxation is one of the main approaches to the taxation of large companies. For example, at the beginning of the 20th century, Germany used special rules of tax regulation for major corporations [7]. In 1942, tax legislation in the U.S. established a special regime for corporate groups to submit a consolidated tax return [8]. Currently, group taxation is applied in 18 countries of the European Union (EU) and 21 members of Organization for Economic Cooperation and Development (OECD) [9].

Scientists have not yet reached a unanimous opinion concerning the concept of consolidated taxation. Some authors think that a group of companies can consolidate the financial results of individual participants and of all its participants [10–12].

In the works of other scientists, consolidated taxation refers to defining the general tax base by summing the financial results of all members of the group of companies [13–15].

In Russia, consolidated tax base is calculated on the basis of the amount of all profits and the amount of all expenses of the participants of consolidated groups of taxpayers (CGT)¹.

The hypothesis of our research is as follows: a mechanism for calculating the tax base by consolidated taxpayers opens up additional opportunities for optimizing taxation; such optimization will naturally lead to a shortfall in the revenues of regional budgets.

Methodological framework of our study includes the works of foreign and domestic scientists on the issues related to the cooperation between government and business and the general principles of the tax system contained in the tax legislation of the Russian Federation.

We conduct our analysis on the example of the Vologda and Lipetsk oblasts, because Vologda Research Center of the Russian Academy of Sciences (VolRC RAS) has been monitoring the situation on the parent enterprises of the largest iron and steel corporations operating within these territories since 2011. Based on the data we have collected, we tried to analyze the work of specific CGT formed on the basis of these corporations. The official data of the Federal Tax Service contains only general information about consolidated groups of taxpayers and does not point out the specific companies under which they operate. Therefore, such scarce information sources make it very difficult to analyze the work of CGT in all of the Russian regions.

Our research uses the reports by the Federal Tax Service, Federal Treasury and Federal State Statistics Service. We also use public statements available at the official websites of metallurgical corporations PAO Severstal (Severstal) and PAO Novolipetsk Steel (NLMK)².

Problem statement

May 7, 2018, Russian President Vladimir Putin signed a decree defining the country's national development priorities for a six-year period³. It is the budget that will largely determine what funds and mechanisms are necessary to finance the activities under this decree; and the implementation of these activities will require 8 trillion rubles of additional funds.⁴

The practice of implementing the presidential decrees of May 7, 2012 suggests that most of the funding will be transferred to the regional level. All the more so since the Russian Government resumed its policy of accumulating oil and gas revenues in sovereign funds: for instance, while the amount of money in the National Welfare Fund decreased by 167 billion rubles from January 1 to June 1, 2017, it increased by 175 billion rubles in the same period in 2018. The forecast of revenues of the Russian Federation budget system up to 2035 suggests that they will decline relative to Gross Domestic Product (GDP) [16].

The state of sub-federal budgets remains tense. As of the end of 2017, budget deficit was observed in 47 out of 85 regions. The level of debt exceeded half of the volume of tax and non-tax revenues in 42 constituent entities of the Russian Federation. Such situation became one of the main factors for reduction of investment and consumer demand.

The destabilizing trends heavily affected the regions, where the largest industrial corporations generating significant cash flows form the basis of the taxable base. It would seem that their presence should create noticeable budget effects. However, the relationship between large companies and the budget in the field of profit tax, one of the most important revenue sources, was characterized by a decrease in the fiscal function of these companies. Summarized data on profit tax revenues from those sectors, in which the main part of the largest taxpayers operate, allowed us to get an insight into the situation. From 2007 to 2016, the volume of payments to the budgets of constituent entities of the Russian Federation decreased in 1.1 times against the background of a twofold increase in profits. At the same time, the share of the largest taxpayers in total tax revenues decreased from 38 to 25 % (Table 1).

¹ Article 278.1 of the Tax Code.

² These corporations prepare their statements on CGT according to Russian accounting standards.

³ On national goals and strategic objectives of the Russian Federation for the period up to 2024. The Decree of the President of the Russian Federation dated May 7, 2018 No. 204.

⁴ Medvedev estimated the expenditures for the implementation of Putin's new May Decree. RBK, 2018, May 8. URL: <https://www.rbc.ru/economics/08/05/2018/5af16d019a79476c127101f5> (date of access: 18.05.2018).

**Inflow of profit tax revenues from the largest economic sectors^{*} to the budgets of constituent entities
of the Russian Federation in 2007–2016, billion rubles^{*}**

Year	Profit	Profit tax	Proportion in the total tax proceeds, %
2007	2325	586	38.3
2008	2176	472	26.3
2009	2095	205	19.2
2010	2773	374	24.7
2011	3564	518	26.9
2012	3472	427	21.6
2013	2934	365	21.4
2014	4232	480	25.3
2015	4390	625	31.6
2016	4532	548	24.9
2016 to 2007, %	194.9	93.5	–13.4 p. p.

^{*} Mining, production of coke and petroleum products, production of chemicals and chemical products, metallurgical production and production of finished metal products.

Source: own compilation with the use of Rosstat, Federal Tax Service, and Federal Treasury data.

Speaking about the reasons for the decline in the participation of large businesses in the mobilization of budget revenues we should take into account that the global environment, in particular the volatility of prices for raw materials, exchange rates, and market demand significantly influence profit generation by economic entities, especially export-oriented ones (which form the majority of large corporations). At the same time, research findings of the expert and scientific community (including the Russian Academy of Sciences) on tax regulation of the largest corporations allow us to conclude that the real reasons lie in the creation of conditions for minimizing taxation, reflected in the legal acts adopted since the early 2000s. Significant legislative changes are as follows: the Russian Federation entered into agreements with offshore countries for the avoidance of double taxation, introduced a zero value-added tax (VAT) rate for exporters, removed the restrictions on cross-border movement of capital and abolished the tax on the dividends received from strategic participation in other companies. According to VoIRC RAS estimates, the annual losses of the Russian budget from these measures amount to an average of five trillion rubles [17].

The institution of consolidated groups of taxpayers adopted in the Russian tax practice has become one of the most important changes in the tax legislation⁵.

Attempts to create a single taxpayer mechanism in the Russian Federation have been made since the mid-1990s, alongside the work on the development of the Tax Code. However, at that stage, it was decided to abandon the idea of consolidation due to its insufficient elaboration.

We should note that the business community appealed to the Government of the Russian Federation⁶ and pushed for the consolidation of taxpayers mainly to obtain a special regime for the calculation and payment of profit tax, which would reduce the tax burden.

The Russian Union of Industrialists and Entrepreneurs was also among those who proposed to introduce this taxation regime for holding companies. In 2007, it put forward an idea to adopt the relevant bill [18].

As a result, in 2011, Russian President Dmitry Medvedev instructed to put into effect the institution of consolidated tax reporting on corporate tax⁷.

It is worth mentioning that the new tax institution has a narrow focus due to the strict criteria of its formation. Access to consolidation is granted only to those organizations whose annual amount of taxes is at least 10 billion rubles, annual revenue is at least 100 billion rubles, and total assets

⁵ On amending Part 1 and Part 2 of the Tax Code of the Russian Federation due to the establishment of a consolidated group of taxpayers. Federal Law 321-FZ dated November 16, 2011.

⁶ Speech of S.I. Shtogrin, auditor of the Accounts Chamber of the Russian Federation, at the round table of the Federation Council of the Federal Assembly of the Russian Federation December 12, 2017. URL: <http://www.council.gov.ru/media/files/> (date of access: 14.05.2018).

⁷ On budgetary policy in 2012–2014. Budget Address of the President of the Russian Federation to the Federal Assembly of the Russian Federation dated June 29, 2011. URL: <http://www.kremlin.ru/events/president/news/11784> (date of access: 14.05.2018).

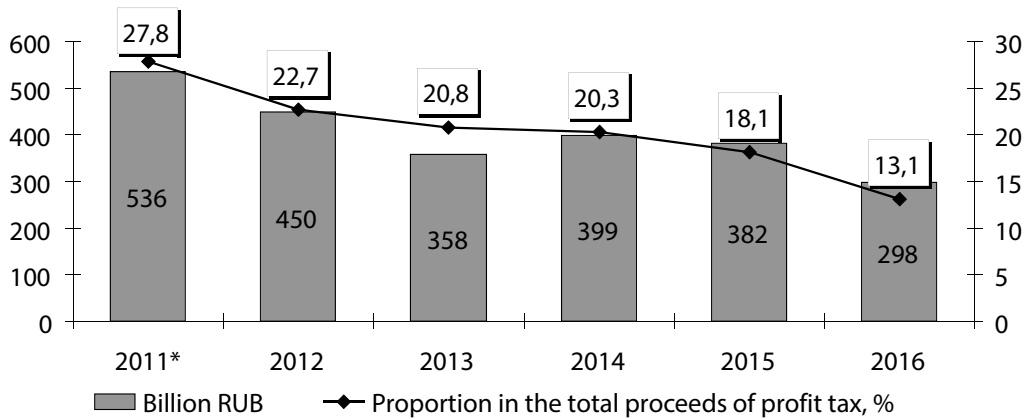
according to the balance sheet is at least 300 billion rubles. In accordance with these criteria, small and medium-sized businesses will not be able to use the new taxation procedure, which puts them at a disadvantage compared to large taxpayers; thus the principle of parity and competitive economic development is violated.

The effects of tax consolidation aroused a lot of criticism. The Accounts Chamber of the Russian Federation in its conclusion reports⁸ on the draft laws on the federal budget annually pointed to a decrease in the revenues from profit tax due to a special procedure for its calculation by consolidated taxpayers. Chairman of the State Duma V. V. Volodin admitted that the introduction of CGT was a mistake⁹. Speaker of the Federation Council V. I. Matvienko did not approve of this measure as well: “How did it happen that after the introduction of such a beneficial measure, the federal budget and the majority of Russia’s constituent entities have lost profit tax? What kind of scam did the state get involved in?”¹⁰

Based on the results of the CTG performance’s analysis for 2012–2016, we make attempted to find out the reasons for such serious criticism of the consolidated taxation system and to assess the implications of its introduction for regional budgets.

Results and discussion

The actual data prove that the first year of CTG functioning was marked by a decline in the inflow of profit tax to regional budgets by 86 billion rubles, or 16 %. In subsequent years, consolidated taxpayers failed to reach the indicators of 2011 (Figure 1).



* The tax paid by those organizations that in 2012 will be included in CGT.

Fig. 1. Inflow of profit tax from the CTG to the budgets of the Russian Federation subjects in 2011–2016 (own compilation with the use of the data of the Federal Tax Service and the Accounts Chamber of the Russian Federation)

In general, the five-year experience of tax consolidation institution’s functioning demonstrated its low efficiency, which was manifested in a twofold drop in both physical and specific volumes of the inflow of income tax revenues to the budgets of the Russian Federation constituent entities.

Having conducted a more in-depth study of the regulatory framework, official data of federal financial agencies and corporate reporting, we identified two main reasons due to which the effectiveness of CGT is low.

The first reason lies in the lack of clear legislative regulation of the mechanism for the distribution of profit tax between consolidated enterprises. In accordance with the legislation, the share of tax that falls on each taxpayer within the group is defined as an average value of the shares of two indicators: the residual value of fixed assets and the average number of employees. At the same time, the responsible participant of CGT independently chooses the criterion for calculating the share and formalizes the choice in the accounting policy.

The application of this procedure, which does not take into account financial performance of the group members, led to an incorrect distribution of profit tax and, accordingly, to budget losses. We find

⁸ Conclusion reports of the Accounts Chamber of the Russian Federation on the draft laws on the federal budget for 2013–2016. URL: <http://www.ach.gov.ru/> (date of access: 18.05.2018).

⁹ Transcript of the meeting of the Board of Legislators of the Russian Federation under the Federal Assembly of the Russian Federation on December 18, 2017. URL: <http://szrf.km.duma.gov.ru/upload/site53/> (date of access: 18.05.2018).

¹⁰ Ibidem.

Inflow of profit tax revenues to the budgets of constituent entities of the Russian Federation from major taxpayers in 2011–2016

Indicator	2011 (before CGT)	After joining the CGT, by years					Average for 2012– 2016
		2012	2013	2014	2015	2016	
AO Karelsky Okatysh (Republic of Karelia)							
Share in the indicators of PAO Severstal, %							
— profit before taxation	30.1	32.3	239.6	x	17.9	12.4	51.4
— cost of fixed assets and the number of employees	not available	8.9	9.1	10.3	9.6	8.2	9.2
Inflow of profit tax revenues to the regional budget, mln RUB	3534	2485	112	0	0	453	610
Share in the total proceeds, %	56.4	47.1	5.1	0	0	10.6	18.2
Main budget parameters of the region							
Endowment with own revenues, % of the national average	100.0	84.2	76.2	72.1	74.2	73.7	78.3
Deficit, mln RUB	159	2244	5886	3717	3777	2618	3648
Debt load, %*	37.1	52.1	72.1	96.3	101.5	100.4	84.9
OAO Stoilensky GOK (Belgorod Oblast)							
Share in the indicators of PAO NLMK, %							
— profit before taxation	60.7	85.9	210.7	99.5	26.0	20.4	53.7
— cost of fixed assets and the number of employees	13.5	14.0	14.6	15.9	15.9	22.1	16.5
Inflow of profit tax revenues to the regional budget, mln RUB	5355	1347	586	1820	110	1274	1027
Share in the total proceeds, %	20.9	7.0	4.3	16.2	0.96	10.5	7.6
Main budget parameters of the region							
Endowment with own revenues, % of the national average	96.1	81.6	76.4	71.9	75.4	71.2	75.0
Deficit, mln RUB	2385	4597	9901	1619	2588	3059	4353
Debt load, %*	35.5	63.4	84.6	82.9	75.1	73.4	76.1

* Debt load is calculated as the ratio of the volume of public debt to the volume of own income.

Source: own compilation using the data of the Ministry of Finance, Federal Treasury, and financial statements of PAO Severstal and PAO NLMK.

a telling example in the situation concerning AO Karelsky Okatysh and OAO Stoilensky GOK that are the key resource assets of Severstal and NLMK, as well as participants of CGT such as PAO Severstal and PAO NLMK. Before their inclusion in CGT, both enterprises had the status of major budget revenue generating enterprise for the regions of their presence (Table 2).

For several years since Karelsky Okatysh joined PAO Severstal's consolidated group of taxpayers, the budget of the Republic of Karelia lost an average of 3 billion rubles per year, or 83 % of the revenues from profit tax proceeds. The average annual damage that the budget of Belgorod Oblast suffers after OAO Stoilensky GOK joined the consolidated group of taxpayers of PAO NLMK is estimated at 4.3 billion rubles, or 81 % of the level of 2011. At the same time, the main resource assets of Severstal and NLMK provided more than half of the profits of the corporations. However, due to the fact that the share of these enterprises averaged from 9 to 16.5 % in the production indicators of the group (the residual value of fixed assets and the average number of employees), less payments were made to their home regions.

The dramatic reduction in profit tax revenues resulted in a sharp deterioration of the state of regional budget systems in 2012–2016 compared to the level of 2011:

— budget self-sufficiency decreased: in the Republic of Karelia — from 100 % to 78 %; in Belgorod Oblast — from 96 % to 75 %;

Translation

– budget deficit increased: in the Republic of Karelia – in 23 times (from 0.2 to 3.6 billion rubles); in Belgorod Oblast – in 1.8 times (from 2.4 to 4.4 billion rubles);

– debt burden of the budget increased: in the Republic of Karelia – from 37 % to 85 % (in 2015–2016 to more than 100 %); in Belgorod Oblast – from 35 % to 76 %.

We can say that after their major enterprises joined the consolidated group of taxpayers the regions ceased to receive the proper return on their financial results achieved through the use of natural, human resources and infrastructure of the territories.

In general, taxation consolidation caused a dramatic redistribution of profit tax revenues between the regions (Table 3).

Table 3

Dynamics of the change in the inflow of profit tax revenues to the budgets of the Russian Federation constituent entities in connection with the establishment of CGT

Indicator	Dynamics of the change in the inflow of profit tax revenues, broken down by years					
	2012	2013	2014	2015	2016	2016 to 2012, %
Increase in proceeds						
Number of Russia's constituent entities	56	60	52	34	32	57.1
Tax revenues, billion RUB	52.6	44.0	61.9	32.5	28.2	53.6
Decrease in proceeds						
Number of Russia's constituent entities	18	23	31	48	51	283.3
Shortfall in revenues, billion RUB	60.8	65.2	127.0	125.9	112.2	184.5
Net losses	8.2	21.2	65.1	93.4	84.0	10.2 times

Source: own compilation with the use of the Federal Tax Service data.

In 2012–2016, there was a twofold decrease in the number of regions where the inflow of profit tax revenues increased, and the number of regions with low dynamics grew threefold. Because of this redistribution, the net loss of tax revenues has increased from 8 to 84 billion rubles a year.

Besides Belgorod Oblast and the Republic of Karelia, there are some other regions, in which the revenues from the operation of CGT decreased by more than a billion rubles. These regions include the cities of Moscow and Saint Petersburg, Krasnoyarsk and Perm krais, Tyumen, Volgograd and Nizhny Novgorod oblasts. In all fairness we should note that the Russian Government has taken a number of measures to partially compensate for the shortfall in regional budget revenues with the help of subsidies, but these are one-time measures that cannot compensate for the shortfall in tax payments. In our view, in this case systematic work should be carried out through the development and approval of a methodology for forecasting shortfall in revenues and redistribution of relevant subsidies between regions on this basis.

The second and, in our opinion, the most significant reason for the low efficiency of tax consolidation lies in the fact that the profits are set off against the losses received by the participants of CGT.

We can observe negative trends in this mechanism if we review the changes in the overall dynamics of the tax base of CGT (Figure 2).

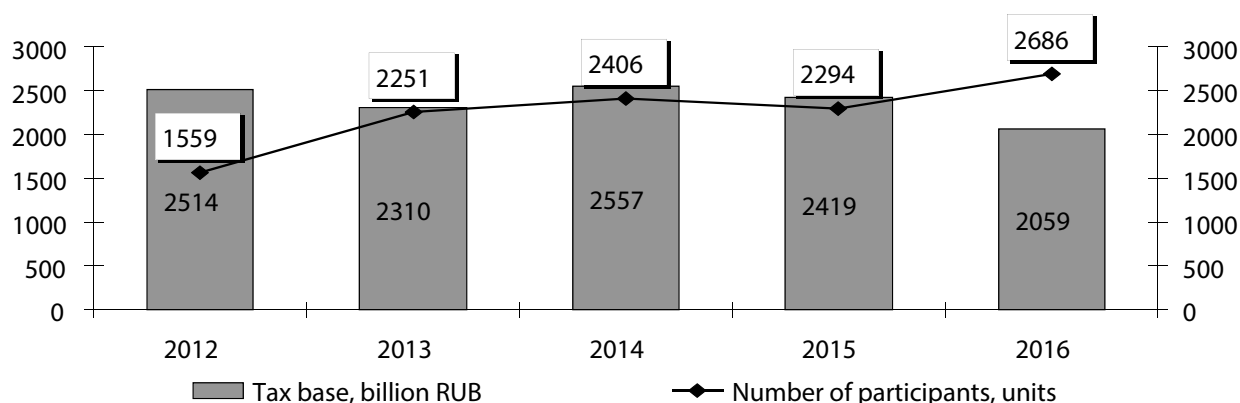


Fig. 2. Dynamics of the tax base and the number of CGT participants in 2012–2016 (compiled in accordance with the Federal Tax Service data)

During 2012–2016, against the background of the 70 % growth of participants of CGT, their tax base decreased by 18 %. In general, the amount of taxation decreased in half of the regions by 917.5 billion rubles, or by 45 %. At the same time, the decrease by more than 836 billion rubles or by 90 % was observed in industrial centers (Table 4).

Table 4

Russia's constituent entities with the declining dynamics of the tax base of CGT

Constituent entity	2012		2016		2016 to 2012, %	
	Number of participants, units	Tax base, billion RUB	Number of participants, units	Tax base, billion RUB	Number of participants, units	Tax base, billion RUB
Yamalo-Nenets Autonomous Okrug	47	286.1	55	220.6	117.0	77.1
Perm Krai	29	30.7	46	21.5	158.6	70.2
Republic of Komi	44	56.5	63	38.1	143.2	67.3
Volgograd Oblast	34	30.7	58	19.6	170.6	63.7
City of Moscow	102	784	228	458	223.5	58.4
Krasnodar Krai	53	58	70	31	132.1	53.4
Moscow Oblast	47	46.9	84	24.4	178.7	51.9
Republic of Sakha	16	48	23	21	143.7	43.7
Samara Oblast	41	76.5	68	30.2	165.9	39.5
Irkutsk Oblast	23	49.7	38	15.7	165.2	31.5
Khanty-Mansi Autonomous Okrug	31	303	44	54	141.9	17.8
Total	467	1770.1	777	934.1	166.4	52.8
All the constituent entities of the Russian Federation	889	2017.2	1353	1099.7	152.2	54.5

Source: Federal Tax Service.

The data obtained suggest that the absence of restrictions on the expansion of the number of participants in consolidated groups¹¹ contributed to their significant growth alongside the opposite dynamics of the tax base. Hence, we can assume that the introduction of new participants in the composition of CGT was made in order to optimize taxation.

The work of the CGT of PAO Severstal can serve as a telling example of how the balanced mechanism operates. Anticipating the results of the analysis of the formation of profit tax in the CGT of PAO Severstal, we should emphasize that the sharp drop in payments from iron and steel enterprises that had generated about 40 % of all tax revenues of the regional budget before the crisis of 2009 became a decisive factor in many issues of the budget system of the Vologda Oblast, primarily the debt problem (Figure 3).

According to the estimates of the regional authorities, the establishment of CGT in the iron and steel sector would help replenish the regional budget by 2 billion rubles and deal with an acute debt crisis. However, the consolidation did not bring the desired result: in 2012–2016, the average annual profit tax levies from CGT amounted to 1 billion rubles against 6.2 billion rubles before the formation of the group (Figure 4).

Thus, the budget of the Vologda Oblast has not received the expected rise in tax payments; moreover, it lost 5 billion rubles annually. At the beginning of 2017, the debt burden amounted to two-thirds of own revenue sources and exceeded the level of 2009.

The introduction of the institution of consolidated groups of taxpayers was accompanied by changes in a number of legal acts regulating the work of joint stock companies. These changes affected the organizational status as well as the presentation and disclosure of information. We can reduce the innovations of the legislation to the following two points.

¹¹ A moratorium on the creation of new CGT and on changing their composition was imposed by Federal Law of November 24, 2014 No. 366-FZ "On amending Part 2 of the Tax Code of the Russian Federation and certain legislative acts of the Russian Federation".

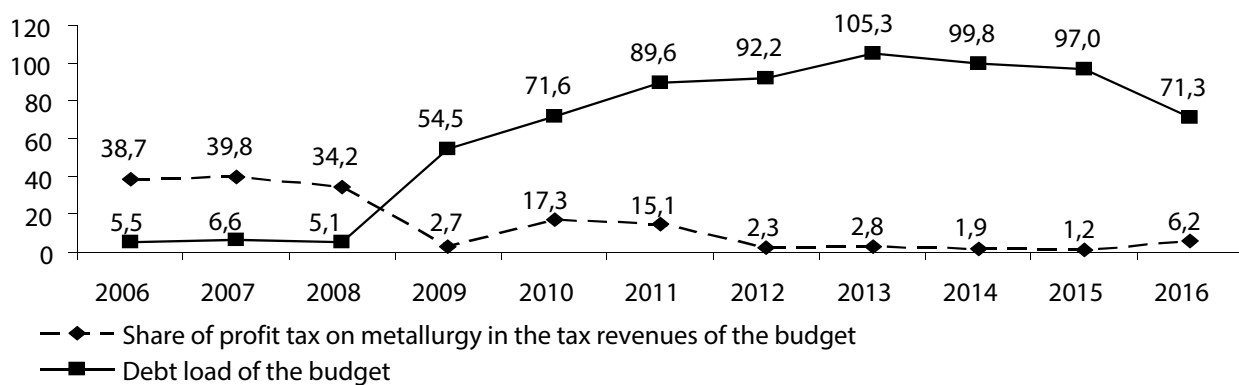


Fig. 3. Dynamics of the share of iron and steel production in the tax revenues and the debt burden of the Vologda Oblast budget in 2006–2016, % (own compilation according to the data of the Ministry of Finance of the Russian Federation, Federal Tax Service, and Federal Treasury)

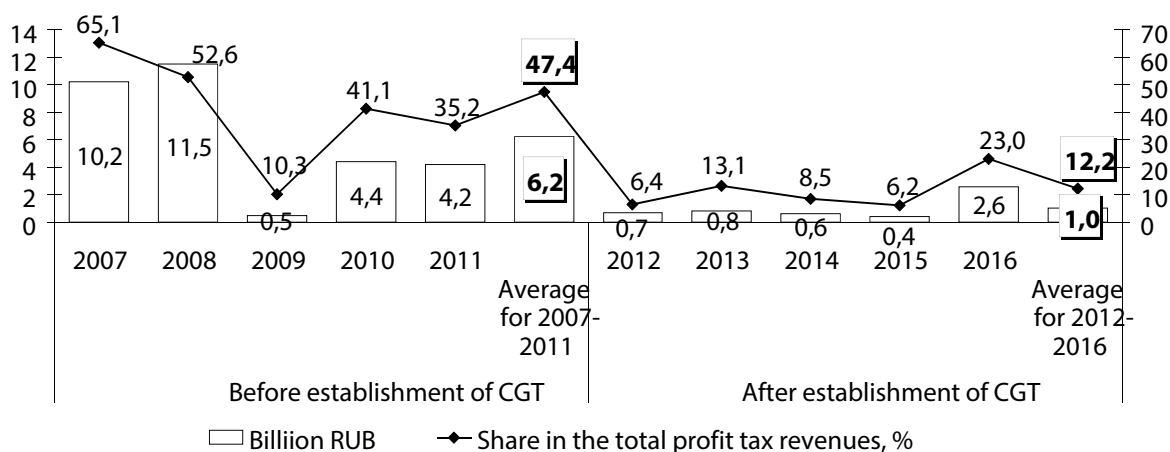


Fig. 4. Inflow of the revenues from profit tax paid by iron and steel enterprises to the budget of the Vologda Oblast in 2008–2016 (own compilation according to the data of the Federal Tax Service)

First, joint-stock companies, instead of being divided into open and closed, are now divided into public and non-public ones. A public company is a company whose shares are publicly placed or publicly traded on the terms established by securities laws. Accordingly, joint-stock companies that do not meet these conditions are recognized as non-public ones.

Second, the obligation of non-public companies that were previously open joint stock companies to publish financial statements has been abolished¹².

These legislative changes had a negative impact on the transparency of the joint-stock companies' activities. Thus, since 2014, out of the 22 participants of CGT PAO Severstal, only the head plant and AO Karelsky Okatysh make their financial statements publicly available. As a result, the group's financial performance and therefore its tax base components are not available to analysts. However, with the help of the List of Russian Organizations portal¹³ it became possible to analyze the financial performance of 15 members of the group from 2012 to 2016. According to the most approximate calculations¹⁴, total profit before taxation for the period amounted to 285 billion rubles, from which it would have been possible to calculate more than 50 billion rubles of profit tax. The actual amount of payments that the budget of the Vologda Oblast received was ten times less than the estimated value (Table 5).

The results of 2014 provide a telling example of the use of a balanced mechanism in CGT PAO Severstal. According to the end of the year, the group lost 13 billion rubles due to the losses that

¹² On recognizing the Order of the Ministry of Finance of the Russian Federation dated November 28, 1996 No. 101 "About the order of publication of financial statements by open joint stock companies" as invalid. Order of the Ministry of Finance of the Russian Federation dated June 5, 2014 No. 45n.

¹³ See: <http://www.list-org.com/?search=all> (date of access: 20.05.2018).

¹⁴ We make the following reservation: we cannot say for sure that our calculations are accurate, since the information available makes it very difficult to define the share of the tax which is due to participants of CGT. Taking into consideration the fact that the share of Cherepovets Steel Mill, being a responsible participant of CGT, makes two-thirds of the industrial base of the entire corporation, we were able to make calculations, not taking into account the shares of other enterprises within the group.

Table 5

Profit before taxation and profit tax for members of CGT PAO Severstal for 2012–2016, million rubles

Indicator	Values of the indicator, by years					Total for 2012–2016	Average for 2012–2016
	2012	2013	2014	2015	2016		
Profit before taxation							
Cherepovets Steel Mill — responsible member of CGT	16341	9170	–37710	44261	106522	138585	27717
OOO Kholdingovaya Gornaya Kompaniya	21782	4687	12153	28565	6307	73555	14711
AO Karelsky Okatysh	10365	11498	9443	7006	13498	51810	10362
OAo Severstal-metiz	713	2323	1097	938	2311	7382	1476
AO Olkon	3378	1445	–247	–1164	–843	2568	514
Others	3594	5111	2375	3656	–3628	11108	2222
Total	56173	34234	–12889	83263	124227	285008	57002
Calculated profit tax*	10111	6162	–2320	14987	22361	51301	10260
Actually received tax	702	783	643	408	2626	5162	1032
Difference between calculated and actual tax	9409	5379	–2963	14579	19735	46139	9228

* We calculated profit tax at the rate of 18 % in the part that goes to the budget of the constituent entity of the Russian Federation.

Table 6

Profit of CGT PAO NLMK and the inflow of profit tax payments to the budget of the Lipetsk Oblast in 2012–2016, million rubles

Indicator	Values of the indicator, by years					Total for 2012–2016	Average for 2012–2016
	2012	2013	2014	2015	2016		
Profit before taxation							
NLMK– responsible member of CGT	24223	–10374	23305	58166	47317	142637	28527
OAo Stoilensky GOK	24447	28301	37997	20829	15684	127257	25451
OAo Altai-Koks	4430	1939	1768	6221	4992	19351	3870
OOO NLMK Overseas Holdings	–14	3163	25772	18964	–28167	19717	3943
OOO VIZ-Stal	18	–988	1372	8601	5491	14494	2899
Others	353	276	322	478	465	1894	379
Total	53457	22316	90537	113259	45782	325351	65070
Calculated profit tax*	9622	4017	16297	20387	8241	58564	11713
Actually received tax	4038	4222	8109	13072	10294	39735	7947
Difference between calculated and actual tax	5584	–205	8188	7315	–2053	18829	3766

* We calculated profit tax at the rate of 18 % in the part that goes to the budget of the constituent entity of the Russian Federation.

Cherepovets Steel Mill sustained as a result of the costs of the American division's liquidation. These losses amounting to 38 billion rubles exceeded 24.8 billion rubles of the total profits of other participants of CGT. If the regime of tax base consolidation did not operate, then the budget of the Vologda Oblast could have received 2.7 billion rubles and the budget of the Republic of Karelia could obtain 1.7 billion rubles, calculated by enterprises independently.

Offsetting the financial results also took place in CGT PAO NLMK; consequently, the budget of Lipetsk Oblast did not receive about 4 billion rubles of profit tax payments annually (Table 6).

Thus, if we proceed from the values of the indicators calculated, then the annual budget losses due to the use of the mechanism for summing profits and losses in CGT PAO Severstal and CGT PAO NLMK are estimated at 13 billion rubles, including the following losses:

- the budget of the Vologda Oblast lost 9.2 billion rubles or 22 % of tax revenues;
- the budget of the Lipetsk Oblast lost 3.8 billion rubles or 10 % of tax revenues.

It is appropriate to emphasize that there are certain specific features in the tax administration of major taxpayers within the specialized interregional inspections located in Moscow. In this case

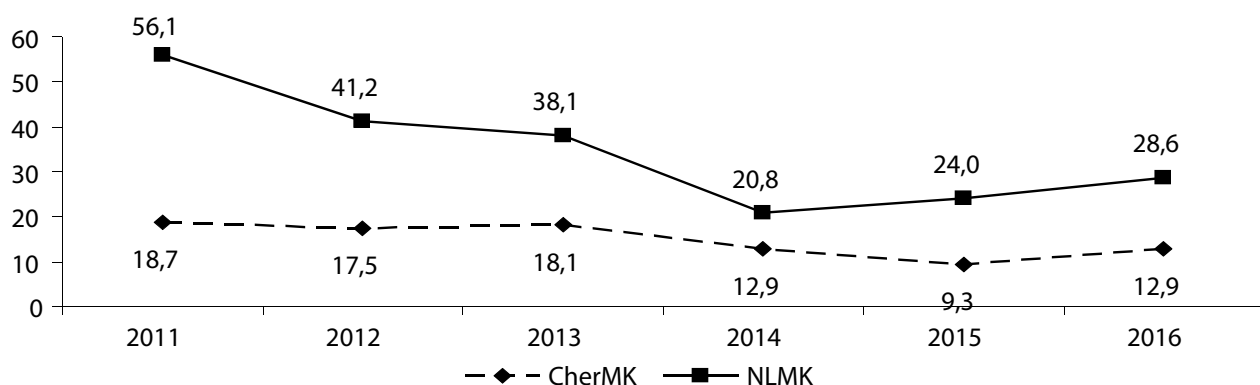


Fig. 5. Fixed capital investments of Cherepovets Steel Mill (CherMK) and Novolipetsk Steel (NLMK) in 2011–2016, billion rubles
Source: financial statements of PAO Severstal and PAO NLMK.

the financial performance of CGT remains out of reach of regional authorities and affects appropriate budget planning.

For example, due to the lack of reliable information on the tax base of CGT Severstal, Vologda Oblast found itself in a paradoxical situation: since 2014, Vologda Oblast' Government does not consider metallurgical production as the main catalyst for the financial resources of the region's economy and does not include the profit indicators of CGT Severstal in the forecast of socio-economic development, and the draft budget is formed taking into account the inflow of profit tax from the group, while this inflow does not have any economic substantiation. As a result of this mismatch, actual proceeds from the consolidated group of taxpayers in 2014–2016 were 60 % higher than the planned ones [19].

Tax optimization has not led to the intensification of investment activities of the responsible parties within the analyzed CGT. As of the end of 2016, capital investments of Cherepovets Steel Mill and NLMK decreased by 30 % and 50 %, respectively, compared to the level of 2011 (Figure 5). It is still very difficult to talk about the modernization orientation of consolidated taxpayers.

At the same time, legal schemes to minimize tax liabilities, through the consolidation regime as well, were used to accumulate significant amounts of profit remaining after taxation (net profit); and this profit was subsequently allocated to dividend payments, the lion's share of which (80 %) was received by the owners of corporations (Table 7).

Table 7

Net income, taxes paid and the dividends of major owners of metallurgical corporations in 2011–2016, billion rubles

Indicator	Values of the indicator, by years						2016 to 2011, %
	2011	2012	2013	2014	2015	2016	
PAO Severstal							
Net profit (loss)	(1.9)	14.6	8.1	(13.1)	40.1	84.7	X
Taxes paid to the regional budget*	7.4	4.1	4.5	4.3	4.6	6.9	93.2
Dividends	12.7	7.6	5.5	48.9	39.1	53.5	421.3
% of taxes	171.6	185.4	122.2	1137.2	850.0	775.4	+603.8
PAO NLMK							
Net profit (loss)	34.7	21.3	(12.8)	19.9	49.9	36.4	104.9
Taxes paid to the regional budget*	9.5	8.8	9.1	13.6	17.9	15.0	157.9
Dividends	10.3	3.2	3.4	12.5	35.6	46.4	450.5
% of taxes	108.4	36.4	37.4	91.9	198.9	309.3	200.9

* Profit tax, individual income tax, corporate property tax, transport tax, and land tax.

Own compilation with the use of financial statements of corporations and the Federal Tax Service.

These data show that in 2012–2016 against the background of falling tax payments, the dividends of the owner of Severstal increased in 4.2 times. Iron and steel enterprises of Lipetsk Oblast increased their contributions to the budget in 1.6 times, but this figure is not comparable to the growth of dividends of the PAO NLMK owner in 4.5 times. At the same time, the nominal amount of dividends paid to the main shareholders of corporations outnumbered the amount of taxes paid.

Thus, we can say that the benefits of consolidation are obvious for its participants, rather than for the budget.

Conclusion

The five-year practice of tax consolidation has shown that the institution of consolidated groups of taxpayers fell short of expectations: it did not contribute to the fair distribution of profit tax revenues between regional budgets, reduced the accuracy of planning the revenue part of regional budgets and did not promote the growth of entrepreneurial activity. In fact, CGT is another tax preference lobbied by a narrow circle of business structures, which a priori did not allow us to expect the growth of revenue sources of sub-federal budgets.

Negative implications of the CGT introduction and the ways to overcome them are reflected in the scientific literature [20–26]. The issue concerning the need to develop effective mechanisms for regulating CGT was from time to time included in the agenda of the organizational structures' meetings of the Federal Assembly of the Russian Federation. As a result, a moratorium on the creation of new CGT has been established, a 50 % restriction on the accounting of losses in the calculation of profit tax has been introduced, and the losses due to a shortfall in the revenues of regional budgets have been partially reimbursed. However, these measures were non-recurrent and they could not compensate for the damage that the budgets suffered.

At the meeting of the Government of the Russian Federation held on June 14, 2018, Prime Minister Dmitry Medvedev announced the abolition of the institution of CGT in 2023.¹⁵ Consequently, 16 currently operating consolidated groups will work for another five years and affect budget interests of a significant number of regions; this fact does not remove the issue of minimizing tax risks from the agenda. To this end, in our opinion, it is expedient to implement the following measures:

1) adjust the formula for the distribution of the tax base by regions so that the formula would calculate the share of profit of CGT's particular participant: the indicator of the share of the depreciable property's residual value of the CGT's regional participant, the indicators of the wage fund's share and the average number of employees of the CGT's regional participant at the same time in equal shares;

2) preserve the restrictions on the deduction of the losses that the unprofitable members of the group bore, in the amount of 50 % of the profits of the profitable participants. According to the estimates of the Accounts Chamber of the Russian Federation, additional inflow of profit tax revenues to the regional budgets could be as follows: in 2018 — 32.2 billion rubles; in 2019 — 34.6 billion rubles, in 2020 — 37.6 billion rubles¹⁶;

3) the federal budget should compensate for the shortfall in the revenues of regional budgets caused by the CGT's activities. Based on the average annual amount of profit tax losses for 2014–2016, the amount of compensation will be 122 billion rubles. In the future, as already mentioned, it is necessary to build mechanisms for redistribution of revenues between regions, depending on the fiscal potential of each constituent entity of the Russian Federation;

4) ensure the access of financial agencies' officials of the Russian Federation constituent entities to the information on the taxpayers who are part of CGT, as currently such information relates to tax secrecy; this measure will increase the accuracy and transparency of budget planning.

References

1. Glazyev, S. Yu. (04.02.2013). Iz-za lobbirovaniya chastnykh interesov izvrashchaetsya promyshlennaya politika [Industrial policy becomes perverted because of lobbying for private interests]. *Kommersant Dengi [Commerzant Money]*. Retrieved from: <https://www.kommersant.ru/doc/2111322> (Date of access: 12.07.2018). (In Russ.)
2. Dobroleja, E. V. (2011). Vovlechenie finansovykh resursov krupnykh korporatsiy v sotsialno-ekonomicheskiy potentsial rossiyskikh regionov [Implication of large corporations' financial resources into socio-economic potential of Russian regions]. *Natsionalnye interesy: priority i bezopasnost [National Interests: Priorities and Security]*, 7(36), 59–63. (In Russ.)
3. Nefedkin, V. I. (2016). Ekonomicheskaya vlast krupnykh korporatsiy i razvitie regionov [The economic power of large corporations and regional development]. *Voprosy ekonomiki*, 3, 99–114. (In Russ.)
4. Pachina, T. M. & Pochivalova, G. P. (2005). Eksterritorialnost kapitala syrevykh korporatsiy: regionalnyy aspekt [Capital's exterritoriality of mineral corporations: regional aspect]. *Problemy prognozirovaniya [Studies on Russian Economic Development]*, 5, 85–96. (In Russ.)

¹⁵ The Government abolishes the institution of consolidated groups of taxpayers. *Vedomosti*, 2018, June 14. URL: <https://www.vedomosti.ru/economics/news/2018/06/14/772751-pravitelstvo-likvidiruet-institut-konsolidirovannih-grupp-nalogoplatelshchikov> (date of access: 14.06.2018).

¹⁶ Conclusion reports of the Accounts Chamber of the Russian Federation on the draft law "On the federal budget for 2018 and for the planning period of 2019–2020. URL: <http://www.ach.gov.ru/> (date of access: 20.05.2018).

5. Povarova, A. I. (2014). Relationship between metallurgical works and the budget: debt increases, taxes decline. *Ekonomicheskie i sotsialnye peremeny: fakty, tendentsii, prognoz [Economic and Social Changes: Facts, Trends, Forecast]*, 6(36), 159–182.
6. Masui, Y. (2004). International Fiscal Association 2004 Vienna Congress, General Report: Group Taxation. *Cahier de droit fiscal international*, 89b, 21–67.
7. Weingast, B. R. (2009). Second generation fiscal federalism: The implications of fiscal incentives. *Journal of Urban Economics*, 65, 279–293. DOI: <https://doi.org/10.1016/j.jue.2008.12.005>.
8. *Worldwide Tax Summaries Corporate Taxes 2015/16*. Retrieved from: <http://www.pwc.com/gx/en/services/tax/corporate-tax/worldwide-tax-summaries/downloads.html> (Date of access: 28.05.2018).
9. Zolotareva, A. B. (2017). *Napravleniya sovershenstvovaniya instituta konsolidirovannoy gruppy nalogoplatelshchikov [Directions of improving the institution of a consolidated group of taxpayers]*. Retrieved from: <https://socionet.ru/~cyrcitec/rnp-pdf/wpaper/031713.pdf>. (Date of access: 28.05.2018). (In Russ.)
10. Nerudova, D. (2009). Methods of consolidation under common consolidated corporate tax base. *Journal of International Business and Economics*, 9(3), 47–48.
11. Parolini, A., Bechara, C., van Hilten, M., Kruger, D., Millar, R. & Sinfield, G. (2011). VAT and Group Companies. *Bulletin for International Taxation*, 65(6), 349–362.
12. Haffert, L. & Mehrtens, Ph. (2013). From Austerity to Expansion? Consolidation, Budget Surpluses, and the Decline of Fiscal Capacity. *MPIfG Discussion Paper 13/16*, 32.
13. Breton, A. (1996). *Competitive Governments: An Economic Theory of Politics and Public Finance* (pp. 178–195). Cambridge: Cambridge University Press, 404.
14. Martinez-Vazquez, J., Jameson Boex, L. F. (1997). *Fiscal Capacity: an overview of concepts and measurement issues and their applicability in the Russian Federation*. Georgia State University, 22. DOI: <http://dx.doi.org/10.2139/ssrn.470821>.
15. Boadway, R., Shah, A. (Eds.). (2007). *Intergovernmental fiscal transfers: principles and practice*. Washington D.C.: The World Bank, 624.
16. Kudrin, A. L. (2017). Reformy dolzhny vyvesti na pervyy plan chastnyy initsiativu [The reforms must prioritize the private sector initiative]. *Rossiyskiy investitsionnyy forum — 2017 [Russian Investment Forum — 2017]*, 34–37. Retrieved from: <http://rusinvestforum.org/magazine/magazine/> (Date of access: 11.07.2018). (In Russ.)
17. Ilyin, V. A., Povarova, A. I. (2016). *Effektivnost gosudarstvennogo upravleniya 2000–2015. Protivorechivye itogi — zakonomernyy rezultat. [Efficiency of public administration from 2000 to 2015. Contradictory outcomes — predictable result]*. Vologda: ISERT RAN, 304.
18. Shokhin, A. N. (2012). *RSPP i tsivilizovanny lobbyizm [Russian Union of Industrialists and Entrepreneurs and civilized lobbying]*. RSPP Publ., 289.
19. Povarova, A. I. (2018). Problems related to regional budgeting amid fiscal consolidation. *Ekonomicheskie i sotsialnye peremeny: fakty, tendentsii, prognoz [Economic and Social Changes: Facts, Trends, Forecast]*, 11(2), 100–116.
20. Smirnov, D. M. (2010). Aktualnye problemy nalogooblozheniya konsolidirovannykh grupp za rubezhom i v Rossii [Actual problems of conjoint groups taxation in Russia and abroad]. *Mezhdunarodnyy bukhgalterskiy uchet [International Accounting]*, 5, 33–39. (In Russ.)
21. Zubarevich, N. V. (2014). *Mezhyudzhetye otnosheniya: ekonomicheskie i institucionalnye aspekty [Intergovernmental affairs: economic and institutional aspects]*. Retrieved from: <https://iq.hse.ru/news/177667731.html> (Date of access: 20.05.2018).
22. Nikitin, K. M., Avdienkova, M. A., Zakharova, O. O. & Gilmanova, E. A. (2016). Konsolidirovannye gruppy nalogoplatelshchikov: kak nuzhno ispolzovat moratoriy [Consolidated groups of taxpayers: how we should use the moratorium]. *Finansovyy zhurnal [Financial Journal]*, 5, 37–51. (In Russ.)
23. Grinkevich, L. S. & Bannova, K. A. (2014). Modernizatsiya sistemy nalogooblozheniya konsolidirovannykh grupp nalogoplatelshchikov [Modernization of the taxation system of consolidated groups of taxpayers]. *Finansy i kredit [Finance and Credit]*, 17, 40–50. (In Russ.)
24. Musaeva, Kh. M. & Abdullaeva, K. M. (2016). Institut konsolidirovannoy gruppy nalogoplatelshchikov v Rossiyskoy federatsii: otsenka i problemy funktsionirovaniya [Institute of the consolidated group of taxpayers in the Russian Federation: the assessment and functioning of the problem]. *Fundamentalnye issledovaniya [Fundamental Research]*, 11–4, 839–845. (In Russ.)
25. Ilyin, V. A., Povarova, A. I. (2014). Problemy regionalnogo razvitiya kak otrazhenie effektivnosti gosudarstvennogo upravleniya [Problems of regional development as the reflection of the effectiveness of public administration]. *Ekonomika regiona [Economy of Region]*, 3, 48–63. (In Russ.)
26. Koroleva, L. P. (2014). Perspektivy sovershenstvovaniya mekhanizma vzimaniya naloga na pribyl organizatsiy v Rossii [Prospects of improvement of organizations in Russia profits taxation mechanism]. *Nalogi i finansy [Tax and Finance]*, 2, 32–39. (In Russ.)

Authors

Vladimir Aleksandrovich Ilyin — Corresponding Member of RAS, Doctor of Economics, Professor, Scientific Director, Vologda Research Center of RAS; Scopus Author ID: 56091499600 (56a, Gorkogo st., Vologda, 160014, Russian Federation; e-mail: ilin@vscc.ac.ru).

Anna Ivanovna Povarova — Senior Research Associate, Vologda Research Center of RAS; Scopus Author ID: 57190409961 (56a, Gorkogo st., Vologda, 160014, Russian Federation; e-mail: aip150663@yandex.ru).