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### **New tax system for self-employed persons**

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#### **Abstract**

This article focuses on the problem of identification, determination and management the results of the activities of self-employed citizens. People become self-employed either intentionally because they leave work and improve the welfare on their own or because of the lack of money, low wages, and constant price increase. This is just a little list of reasons why people are seeking secondary earnings. The decision to legalize self-employment and on income tax registration of them had become necessary because the government of the Russian Federation intended to include self-employment in the legitimate economic system and increase confidence in tax audit and in question about source of income which is not subject to tax. 'Self-employed person' is not too far removed from 'entrepreneur', according to foreign study. That is why there is not a clear separation between these words. However, entrepreneur is most often considered as a person who desires to develop own business and has to invest a lot in the early stages. 'Self-employed' is a person who plans to work independently without recruitment and any transactions not only in the early stages but thereafter. There is a well-argued conclusion that innovation of the Russian Ministry of Finance is aimed at primarily increase in fees. It remains to be seen if this novation will improve the situation for self-employed persons.

**Keywords:** tax, taxation, self-employed citizens, tax treatment, entrepreneurship, amendment of legislation, government of the Russian Federation.

#### **Introduction**

Experts of Association of Chartered Certified Accountants (ACCA) consider shadow economy as economic activity and its earned income which outside the system of governance, taxation and supervision. According to the most recent study of ACCA related to assessment and forecast of global shadow economy development, Russia joined the top five and was ranked fourth place among 28 countries. Shadow economy is 33,6 trillion roubles or 39% of the last year's gross domestic product (GDP) of the country. This indicator is about 84% higher than the global average [1].

This difficult situation of increase in people who take part in shadow economy is caused by not only desire to avoid paying taxes but also some objective reasons:

- 1) the high unemployment rate;
- 2) financial burden of employer to pay insurance premiums. That is why they seek to hire illegal employees or pay extra envelope salaries;
- 3) a substantial amount of fixed contributions on a regular basis for individual entrepreneur (at least 32385 rubles in 2018). You have to pay even if there are not business profits;
- 4) the constant changing the pension law and lack of assurance of dignity pension.

All this leads to citizens do not really hope for the government in financial matters and find sources of income on their own. That is why there is the need of such category as self-employment. Dmitry Medvedev, the Russia's Prime Minister, offered to work hard on the legal acts related to self-employment during his speech in the State Duma [2].

## Literature review

The term 'population self-employment' is currently enough popular. A lot of foreign economists have contributed significantly to development an understanding of the complex issues of self-employment, determined its role in economic development and its features in various occupations and also provided direction of further development. For example, T. Bates, J. Blanchflower, R. Boden, J. Williams, P. Clark, M. Taylor's works. However, foreign economists, of course, cannot know and accurately reflect reasons of self-employment development and its specifics in the Russian Federation [3].

Such home-grown economists as V.Abakumov, I. Bugayan, V. Zherebin, N. Kraev, V. Manevich, M. Toxanbayev, M. Udaltsov have contributed to creating different aspects of self-employment. [3]

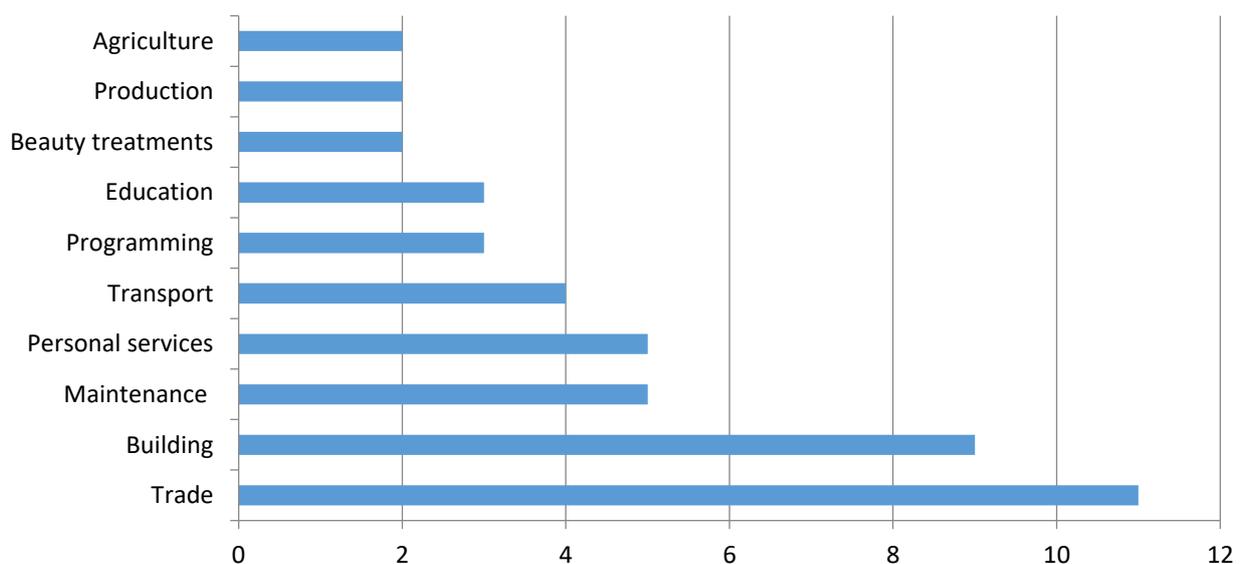
According to the site of the Pension Fund of the Russian Federation, 'self-employed population is individual entrepreneurs, heads and members of peasant (agricultural) households, lawyers, arbitration managers, notaries who practice in the private sector and other persons who practice in the private sector but are not individual entrepreneurs' [4].

## Methods and materials

Notwithstanding the lack of the specific definition of a person who works for himself or herself in the legislation, there are some features which help to determine a self-employed person:

- 1) This person is considered to be unemployed because he or she does not have a permanent place of employment and is not registered as an entrepreneur;
- 2) This person works independently, that is without hired staff;
- 3) This person is really good at his or her work and makes money doing it;
- 4) This person does not transfer taxes, charges to the budget and do not pay insurance premium for pension and health care;
- 5) It is not the licensed line of business [5].

The following figure shows the structure of distribution of this identified category employment, according to the data from the All-Russian Center for the Study of Public Opinion (ACSPo).



**Figure 1:** Areas of self-employed persons's work, % of respondents

- 1) Voluntary registration with the Federal Tax Service on the basis of an application filed by a self-employed person. The main advantages of the self-employment taxation over entrepreneurs are:
  - 2) person. This registration is necessary only for tax on private income relief (art. 217.70 of the Tax Code of the Russian Federation).
  - 3) It is not necessary to operate accounting (self-employed persons do not have to report to the tax authorities and extra-budgetary funds).
  - 4) Self-employed citizens do not need to maintain book-keeping. That is why they do not need to hire an accountant, explore the nuances of book-keeping on their own, process tax register, reports, book of revenue and expenditure accounting.
  - 5) There is a possibility to buy a patent over the convenient period. There are patents which are available for a month or a whole year (the price depends on the period).
  - 6) Self-employed citizens can take part in the programme of tax holidays involving tax and charge exemption until 1 January 2019.
  - 7) It is not necessary to choose between the current tax regimes. They just need to pay for a patent and its price includes the tax payments and charge to the funds [6].

The table 1 shows the points below simplistically.

Table 1: The comparison of self-employed persons and individual entrepreneurs

<b>Criteria for comparison</b>	<b>Self-employed person</b>	<b>Entrepreneurs</b>
Registration	Simplified or automatic after a purchase of a patent	Difficult with different procedures and provision of documents
Amount of the State duty (rub)	100	800
Recruitment	Not allowed	Allowed
Tax record keeping	There are not reports, cash registers and book of revenue and expenditure accounting	It depends on a chosen tax regime
Taxation	Only for a patent, without taxes	There are the general taxation system, single tax on imputed earnings, unified agricultural tax, patent tax, simplified taxation at will

## Results and Discussion

The decision to legalize the activities of self-employed persons and register them with tax accounting appeared because the government of the Russian Federation intended to include self-employment in the legitimate economic system and increase confidence in tax audit and in question about source of income which is not subject to tax.

In opinion of the government, self-employed persons may choose such organizational and legal form of business as individual entrepreneurship but there are some reasons which prevent it:

1. The complexity of the registration with tax accounting;
2. There are a lot of problems related to the administrative authority;
3. There is a risk of loss of property because of fulfilment of the obligations.

That is why the programme for allowance will be adopted (probably temporary):

1. The low-cost procedure for exercising of entrepreneurial activity;
2. The rejection of tax audit with respect to the new individual entrepreneur and of requirement of accountability;
3. The equal conditions of administrative responsibility with physical persons;
4. The possibility to buy a patent for a period of less than a whole year.

The cost of a patent will be determined by the local power. These funds will become a part of the budget of the region. However, law makers were encouraged to fix price not over 20 thousand rubles. 10 thousand rubles of this amount will be directed to the budget of the member of the Russian Federation, 9 thousand rubles to the Pension Fund of the Russian Federation and 1 thousand rubles to the Federal Compulsory Medical Insurance Fund. Authorities will divide this payment into components and promise to meet it within 10 days after payment of a patent.

Let us consider self-employment in the United States for the purpose of a comparative analysis. According to the data from the famous economic and business Internet recourse «Investopedia», it may be deduced that different studies show different results. That is why it is difficult to determine categories of activities which can be put on the list of self-employment. It is estimated that approximately 30% of workers relate to the category of self-employed citizens in the United States.

If a citizen of this country is employed, he or she pays 7,65% of incomes for social security and health insurance and 7,65% are paid by an employer. But in case if a citizen is a self-employed, he or she is an employee and employer at the same time. That is why there the self-employment tax which is equal to 15,3 % in the United States.

The second large tax on self-employment is the federal income tax. Rates of taxes on self-employment are constantly developing and depend on income in the United States. The lowest rate is 10%, it is paid by persons whose income is less than 9225\$ per year. The highest one (36.9%) is for persons who earn more than 414\$ per year [7].

Moreover, self-employed persons' disbursements depend on the taxation of the states and municipalities in the United States. Additional payments make up 5,6 % of self-employed persons' income. Thus, these disbursements in the United States can be more than individual entrepreneurs pay under the simplified system of taxation in Russia. However, the percentage of self-employed persons constantly increases in the United States which has positive effect on average income of the population.

According to the research of the international consulting company McKinsey related to self-employment of the UK economy, 14 million of citizens have chosen self-employment as an organization of their activities. Self-employed persons can work not only on their own but also with other people in this country. This could be a partnership with a limited liability company (LLP). Thus, self-employment is legally identical to business and could be compatible with a principal place of work.

The taxation in the Great Britain is similar to the taxation in the United States. There is the income tax in the Great Britain which depends on income and social insurance tax (to social funds) [8].

Table 2: The dependence of tax on income in the Great Britain

<b>Income</b>	<b>From £0 to £11,850</b>	<b>From £11,851 to £46,350</b>	<b>From £46,351 to £150,000</b>	<b>Over £150,000</b>
Income tax	0%	20%	40%	45%

According to the data of the table 2, there is a progressive rate of the taxation in the Great Britain and the higher self-employed person's income, the higher percentage of a tax. There is the similar system of self-employed persons' taxation in Canada. Attention should also be paid to the government policies related to self-employment, despite the fact that this system is not fundamentally different in comparison to the previous countries. Self-employed immigrants are in demand as people with high demand occupations or entrepreneurs. There is the special programme of immigration for self-employed persons in Canada. This programme allows a citizen of any country to obtain a residence permit if this person speaks English well, has an experience as a self-employed in the country and money to pay for this programme (from 1540\$).

However, if a person wants to take part in this programme, he or she must have a relevant experience in the field of their activities, for example, participation in cultural or sporting events at the global level. According to the conditions of this programme, not every self-employed person seizes the opportunity because the list of a series of professional activities which the country acutely needs is limited. This list of desired professions includes people who can contribute to the development of the cultures of the state (actors, musicians, florists and etc).

Self-employed persons need to comply with the selection criteria which determine the compulsory minimum points for a citizen (35 points out of 100). The criteria include education, age (the ages between 21 and 49 are highly appreciated), experience, good knowledge of the English language and so-called ability to adapt [9].

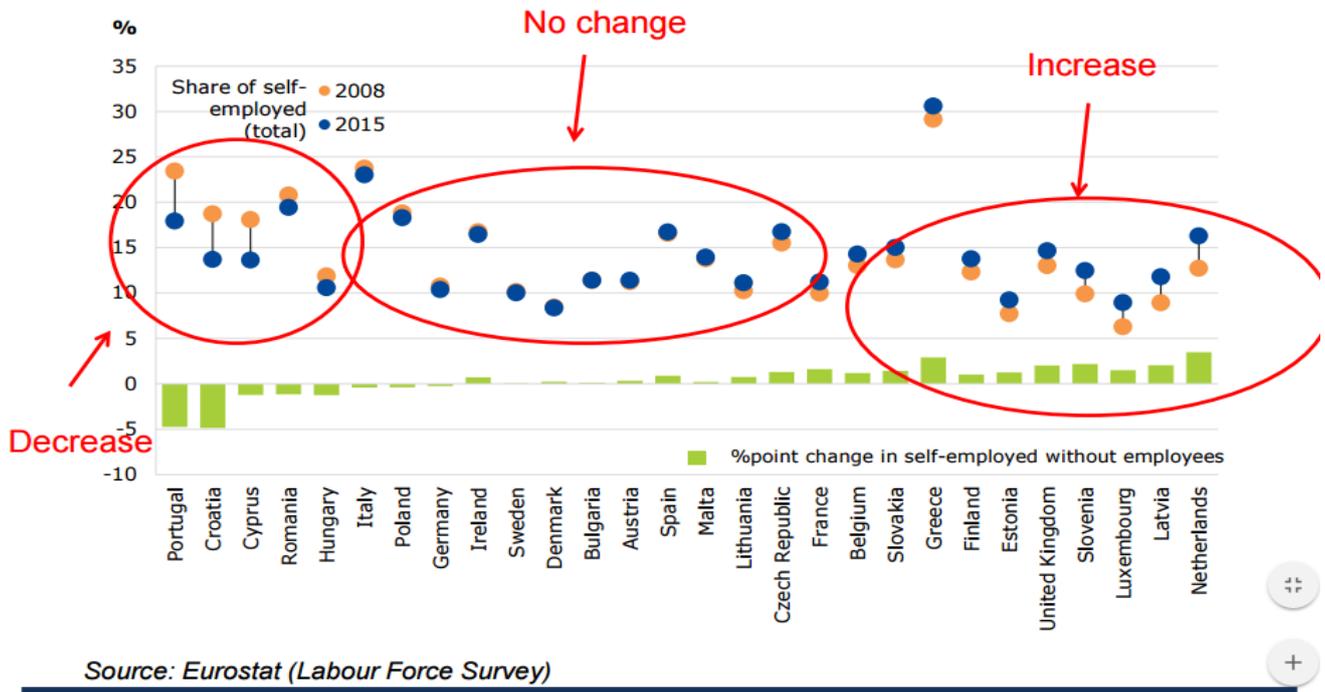
A self-employed person will have the right to take part in this programme only if he or she complies with the mentioned above 2 parameters.

Self-employment is often considered as the main way to make money for most citizens in developing countries, in contrast to the states mentioned above with middle and low-income of the population. For example, approximately 60% of employees are self-employed in Kenya; this indicator is about 70 % in Bangladesh and about 75 % in India. Moreover, the social security and medical programmes do not cover self-employed citizens in most developing countries.

Gary Fields, a Professor of economics of the Cornell University in the United States, says that most of the world's poor people are self-employed. Government policy in developing countries should be designed to increase the number of people who get regular job, instead of self-employment. They are not people who go freelance for pleasure or big money, they are people who, for example, buy cigarettes in bulk and then sell them by the piece to earn a few dollars to eat. In other words, this situation differs from the other one in the United States or in the Great Britain where a self-employed person likes work more than an average staff member of a company. People become self-employed in developing countries because they do not have a choice. [10]

It could be considered this activity maybe came into being before the emergence of a definition of the term 'self-employment'. The legal and tax aspects of self-employment are regulated at the national level in the European Union, though European policymakers want to reduce these systems to a common denominator. There is the division of self-employment and entrepreneurship in some European countries but there is a very different situation in other European countries. Moreover, there is a separate category of 'dependent' self-employed persons which includes people who depend on a contract with a company or with a customer.

Researches of the Eurofund draw attention to the fact that government policy can be considered from different directions with respect to self-employed persons. On the one hand, this category of citizens creates employment on their own with positive effect on economic development and unemployment. On the other hand, a lot of 'freelance' employees try to avoid responsibilities and taxes which are common to company employees. That is why some states try to focus not on the support for self-employed persons but on the fight against false self-employment. This suggestion of the Eurofund shows that government policy related to self-employment should have a lot of aspects.



**Figure 2:** Country differences in trends

This figure shows dynamic of self-employment development in the global economic marketplace of different European countries from 2008 to 2015 [11]. According to that data, the smallest percentage of self-employed persons in Denmark. The highest indicator is in Greece, however, there is not the dynamism. The largest decline in self-employed persons is in Croatia, Portugal, Romania, Cyprus. The largest increase in self-employed persons is in the Netherlands, Latvia, Luxembourg, and Slovenia.

An extensive study was undertaken in the period 2017-2018 to determine the obstacle preventing citizens of the Russian Federation to be legalized in accordance with the different taxation regimes.

The issue of promotion of entrepreneurs to 'emerge from the shadows' is really painful in the country because the previous attempts to legalize self-employed persons have failed.

First, even though the Federal Tax Service provides comfortable opportunities for state registration of any form of ownership and activity in electronic form, the reason for not legalization of income is a need to visit tax authorities and to perform an administrative action related to registration, provision of declaration and etc. People are interested in a system of quick identification, remote interaction with authorities. This is due to the development of modern information technologies which makes it possible to obtain information it in other areas, on the other services, through the Public Services Portal of the Russian Federation.

The second reason is economic losses as a result of the current regimes for self-employed persons including the payment which does not depend on a result of activities. Patent or tax on short-term incomes must be paid even in the absence of income.

The third one is the payment of insurance premiums even at negative levels of income. That is why there is a problem to introduce technologies which allow employees to pay in the extra-budgetary funds in case insurance premiums are included in tax on professional activity.

Thus, the main taxpayers' request is to complete digitalization of the Federal Tax Service. M. Mishustin at the board of the Federal Tax Service said that the fiscal administration will start to integrate information systems in 2018. It will include a system of goods marking, a system of monitoring of value added tax payment, besides online cash registers which give an opportunity to control over mandatory payments in real-time. The Federal Tax Service wants to start this integration with the single registry office. A credible and full registry of citizens should emerge at the disposal of the tax administration, as a result because database of these ministries and administration are different. That is why there is an opportunity to eliminate shadow economy. If the registry is full, there will not be shadow economy and current participants of that economy will be obliged to be legalized or fully involve in the criminal structures.

The problems of decrease in the need for labor with increase in productivity through investment will be solving by expansion of employment in small businesses. The Government is ordered to encourage self-employment especially in regions. The President, in his message to the Federal Assembly, reported that individual entrepreneurs, self-employed persons who use digital service need to be free from accountability and it is also necessary to change payment of taxes to transaction that operates automatically for these persons.

The drafting of a bill on new tax special regime tentatively titled 'tax on occupational income' is in preparation in the Russian Federation. Self-employed people will pay this tax. Rate is 3% if a person provides services to physical persons and 6% to legal persons. The income limit which is being discussed is 10 million rubles per year. Another limitation is the lack of wage earners. There is not a list of authorized activities. The Ministry of Finance offers to approve the list of activities and that income from this list will not be under new special regime, for example, sale of real estate.

4 regions were chosen to test self-employed persons for this pilot project which will start from 1 January 2019 in Moscow, Tatarstan, the Moscow and Kaluga Regions. Tax will be paid using 'ersatz-CRM' (cash register machine). It is a mobile application which will allow to register with tax authorities, to pay taxes without accountability and special documents; it will make biometric identification and show revenues. The remainder of the small business has to start using online cash registers in 2019, for example, entrepreneurs who provide services. The Ministry of Finance decides that this new regime is better than the use of online cash registers.

A self-employed person will add income on his or her own using this mobile application at the end of a month and therefore there will be the monitoring lack of full account of income. That is why the Ministry of Finance relies on consumers who will require a check after payment from self-employed persons. The system of 'points' for requirement of a check is invited to be introduced to encourage consumers because they will be able to pay a part of their taxes using there points. The purpose of an introduction of the tax is to increase in economic transparency. There is the weakness of the innovations because the Ministry of Finance does not understand yet who will pay for pension and treatment of self-employed persons. The administration offers self-employed persons not to pay fixed insurance premiums for the success of this legalization.

Also there is a proposal to provide self-employed persons the tax capital for development at the moment of registration, thus the total payments may decline by about a quarter per year.

S. Katyrin, the President of the Chamber of Commerce and Industry (RF CCI), said that the CCI supports a new proposal of the Ministry of Finance and provision of a tax deduction because it can contribute to legalize self-employment and help self-employed persons 'emerge from the shadows'. The expert recalled that the best

decision of legalization is a cheap patent or payment of low taxes on income. Also, it is important to minimize the formality of registration, process of activities and to give an opportunity to stop doing business without unnecessary paperwork at any time.

## Conclusion

The experts' prospects for the impact of these measures are different from expectations of the ministries. For example, according to FBK Institute for Strategic Analysis Director I. Nikolayev, legalization of self-employment must be provided during economic growth. In this case authorities are more likely to include self-employed persons in taxation. In I. Nikolayev's opinion, self-employed persons will not be interested to give their part of income to the state now.

A. VedeV, the head of the research Centre of the Presidential Academy of National Economy and Public Administration, noted that individual entrepreneurs agree with the concessional programme of taxation now. The aim of the innovations of the ministries is to increase fees, and it is not clear now if they will make better the situation for self-employed persons.

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