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THE AEB GUIDE TO INVESTING IN RUSSIA

Tax incentives for investors in Russia: what's next?

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The investment framework in Russia has significantly changed and to some extent improved in recent years. Russia is currently ranked 31st in the World Bank's 'Doing Business Report',[1] whereby at the time of the ranking's launch a few years ago, Russia occupied 124th place. Russia ranks 53rd in 'Taxation' and is achieving higher positions each year. The ultimate, officially declared goal – to be among the Top 20 in the investment ranking – should make Russia more attractive to investors. Also, tax incentives provided locally in the Russian regions should serve this purpose.

In general, Russian investment legislation provides for a number of protective rules for investors, including, but not limited to guarantees against negative changes in the legislation, compensation in case of nationalisation of property, free transfer of income from Russia, the most-favoured-nation regime,[2] and the grandfather clause. Current Russian legislation provides for various tax incentives that also consider the above principles to certain extent.

Types of tax incentives for investors

First of all, there are incentives associated with certain activities, e.g. 150% R&D super deduction, reduced rates for social security contributions for IT companies, etc. Secondly, there are project-related tax incentives, e.g. Skolkovo (project participants may obtain incentives with respect to VAT, corporate income tax, corporate property tax, and social security contributions).

There are other incentives as well. Both the federal and regional investment promotion laws provide for tax incentives and other measures to support investors, which mostly allow application of reduced tax rates for taxing profits (corporate income tax), property (corporate property tax) or personal income (personal income tax). Also, some non-tax measures may be allowed (low-rated lease payments for land in state ownership, subsidies from the federal or regional budget, financial support through loans or grants from the Industrial Development Fund, etc.). To obtain the benefits, investors generally have to comply with certain requirements, in particular, the project should qual-

[1] https://russian.doingbusiness.org/ru/data/exploreeconomies/russia

[2] The same conditions for doing business compared to Russian companies.

ify as a priority project for Russian authorities (this usually means new technologies, IT, import substitution, development of regional infrastructure, etc.). Also, a minimum investment threshold may be set forth as one of the criteria, or a requirement for the salaries of employees hired for the project to be no lower than the average regional level.

Special investment contracts (SPIC)

Federal Law No. 488-FZ ‘On Industrial Policy’ dated 31.12.2014 introduced the special investment contract (SPIC) as a government support guarantee for major companies investing in technology, the list of which is being approved by the state. SPICs create special benefits and incentives for investors – whether Russian or foreign – to invest in Russia and localise their production. In particular, there may be tax holidays available with regard to corporate income tax and corporate property tax.

Investors enjoy the opportunity to enter into SPICs with authorities at the federal, regional and local levels. Initially, there was a high investment threshold for the federal level (750 million roubles), which is currently abolished. Also, the terms of incentives were extended as a result of amendments to the above law in August 2019. They currently reach up to 15 years instead of 10 years for projects with total investments of up to 50 billion roubles and up to 20 years for projects with total investments exceeding 50 billion roubles. The incentives provided under SPICs concluded prior to the above amendments remain unchanged, so the same rules apply to them as before.

Regional investments project

Another opportunity to receive certain tax and other incentives is the implementation of a regional investment project. Such projects should be aimed at industrial manufacturing of goods and meet the following requirements:

- 100% localisation of production in the relevant constituent entity of the Russian Federation, partial localisation is also allowed with respect to some regions (e.g. Buryatia, Sakha, Tyva);
- At least 50 million roubles capital investment over a 3-year period or at least 500 million roubles over a 5-year period;
- The company does not apply special tax regimes, is not a resident of a special economic zone or located in the territory of priority social and economic development.

Eligible entities obtain a set of benefits that may vary in the regions:

- zero corporate income tax rate;
- application of a reducing coefficient with respect to mineral extraction tax (0, 0.2, 0.4, 0.6, 0.8 depending on the tax period and territory);
- application of increased depreciation rate (up to 2) to fixed assets.

Investing in regions

Russian regions have fairly broad legislative powers and may independently establish both preferential conditions for investors and the procedure and requirements for using such conditions, unless there are limitations set forth by the Tax Code or other federal laws. There are 85 regions in Russia and each one has different regional regulations. So, the benefits offered by the regions are quite diverse and may include lower rates, as well as full or partial exemptions for corporate property tax and land tax. They may also guarantee unchanged tax rates for investors.

In most regions, investors must undergo authorisation with respect to the project in order to obtain tax incentives. For this, submission/approval of a business plan and signing of an agreement with the region are generally required.

Special economic zone (SEZ)

Special economic zones are territories with a special legal status and preferential economic and tax conditions for resident companies. Each special economic zone involves benefits in a certain area of activity. In particular, there are:

- logistics SEZ;
- industrial SEZ;
- technological SEZ;
- tourism SEZ.

There are 27 SEZs in Russia (10 industrial, 6 technological, 10 tourism, and 1 logistics).[3] Residents of such zones enjoy significant tax, customs and economic benefits. They are entitled to pay corporate income tax at a reduced rate varying from 0 to 15.5%, purchase land at a price not exceeding 50% of the cadastral value, and be exempt from import and export customs duties and import VAT on them. Residents may apply a 0% rate for transport, corporate property and land taxes during the first 10 years. In addition, there is a guarantee against adverse changes in the legislation.

Territory of advanced social and economic development (TASED)

There are currently more than 100 TASEDs in Russia and their number continues to increase. TASED residents enjoy the following incentives and benefits:

- reduced corporate income tax rate (established by the constituent entity of the Russian Federation);
- reduced tariffs of social security contributions;
- simplified VAT recovery;
- land tax exemption (in several TASED).

Notably, tax benefits are guaranteed for the entire duration of the residency. To become a TASED resident, an application and a corresponding package of documents must be submitted to the managing company of a certain TASED and a special agreement on carrying out activities must be signed.

'Russian offshores'

These are special administrative areas (SAR) newly introduced by Russian legislation for re-domiciliation of foreign companies to Russia. At the moment, there are only two of them: on Russky Island in the Primorsky region and October Island in the Kaliningrad region. Eventual tax benefits may include reduced tax rates on dividends, proceeds from the sale of shares, etc.

Free Port of Vladivostok (FPV)

From a tax perspective, residents of the FPV are generally entitled to a reduced corporate income tax rate and reduced tariffs of social security contributions. They may also apply incentives in relation to VAT similar to TASEDs.

Considering the above, investors have a lot of opportunities for various projects in Russia and most of them allow the tax burden to be reduced. It is important to start preparations for a project in advance. This should include considering the eventual number of incentives and favourable regimes for which the project could potentially qualify and clarifying the application procedures (if any). Moreover, a project's relevance should be checked from the perspective of sanctions and the presence of further restrictions (some strategic industries have foreign investment restrictions). It is also important to stay updated on continuing and proposed legislative changes. Some insights on this could be taken from a document regularly published by the Ministry of Finance of Russia: the Main Directions of the Budget, Tax and Customs Tariff Policies. For example, the Main Directions of the Budget, Tax and Customs Tariff Policies for 2019 and for the Planning Period 2020 and 2021 describe one of the major directions as creation of stable tax conditions for the oil and gas sector by fixing the existing rules for the next 6 years. Another goal is to achieve certainty in the legislative changes by foreseeing a statutory rule that laws published after a certain date which significantly worsen the taxpayers' position or tax conditions should come into force no earlier than one year later. This should end the existing practice of chaotic adoption of numerous tax laws that amend the existing rules at the end of the year.

In general, it could be concluded that despite complicated political and economic circumstances, Russia remains a fairly attractive place for foreign investments. This is also due to the wide range of support measures and tax incentives. An increase in Russia's investment attractiveness is also highly aspired to at the official level, in particular, due to Russia's expected entry into the Top 20 of the Doing Business rating.

[3] Based on status on 04.09.2019.