



## Russian Far East: Legislative Overview

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## The Russian Far East is one of the few remaining "new frontiers" for development and investment.

It is one of the most significant investment opportunities arising from Russia's increased diplomatic and commercial emphasis on its partners in Asia, together with Russia's earnest focus on the development of and increased investment in the Russian Far East.

Over the past several years, Russia has been developing legislation and administrative structures to open the Russian Far East to increased investment opportunities for foreign investors, particularly in the areas of infrastructure development, ship and oil rig building, trade, production of advanced technology products, tourism, and agriculture with the focus on developing the Russian Far East into a leading international business, energy and trade hub.

Russia's efforts to stimulate investment and growth in the Russian Far East have been showcased at its Eastern Economic Forums held in Vladivostok, Russia. The most recent Eastern Economic Forum, held in September 2017, resulted in 217 investment contracts for over 2.5 trillion roubles (approximately 44 billion US dollars).

In President Putin's welcome statement to the participants of the 2017 Eastern Economic Forum he acknowledged that the "Russian Far East's proximity to the large and rapidly growing Asia-Pacific market, its wealth of resources and unspoilt natural environment, and the unparalleled transport, logistics and industrial potential to be found here are all attracting increasing international attention.... Russia is faced with an ambitious target: to provide the best possible conditions for doing business in the Far East, to launch new manufacturing capabilities, and to create additional jobs. It is with this objective in mind that advanced special economic zones have been set up, offering tax incentives, simplified government regulation and oversight, and extensive infrastructure."

Much of the legislation implementing the incentives for investment in the Russian Far East is already in place, and is likely to be elaborated further in support of Russia's desire to develop the region and attract investors.



### Contacts

Jennifer Josefson, Partner  
Tel. +7 495 228 8502  
e-mail: [jjosefson@kslaw.com](mailto:jjosefson@kslaw.com)

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Our global experience throughout the project value chain gives us an in-depth understanding of the complex interplay among corporate, tax and track structuring and project agreements and how that interplay affects key milestones including development, financing, construction and commercial operations.

## Free Port of Vladivostok

The sea port of Vladivostok is one of the most efficient and effective international sea routes for many countries. The Port of Vladivostok is ice free and was established in 1897.

In the summer of 2015, Russia passed legislation introducing a simplified regime for entering and conducting business within the Vladivostok sea port, the surrounding area of the sea port and certain other territories specified by law (the sea port, its adjacent territory and other territories subject to relevant regime are referred to herein as the "**Vladivostok Free Port**").



As of today, the following territories enjoy the benefits of the Vladivostok Free Port:

in Primorsky region:

- Artemovskiy urban district
- Vladivostokskiy urban district
- Bolshoy Kamen urban district
- Lazovskiy municipal area
- Nakhodkinskiy urban district
- Partizanskiy urban district
- Spassk-Dal'ny urban district
- Ussuriyskiy urban district
- Nadezhdinskiy municipal area
- Shkotovskiy municipal area
- Oktyabrskiy municipal area
- Ol'ginskiy municipal area
- Partizanskiy municipal area
- Pogranichnyy municipal area
- Khasanskiy municipal area
- Khankayskiy municipal area

on Kamchatka peninsula:

- Petropavlovsk-Kamchatskiy urban district

in Khabarovsk region:

- Vaninskiy municipal area

on Sakhalin island:

- Korsakovskiy urban district
- Ulegorskiy urban district

on Chukotka peninsula:

- Pevek urban district

The special regime for the Vladivostok Free Port was established by Federal Law No. 212-FZ "On Free Port of Vladivostok" dated 13 July 2015 ("**Law on Vladivostok Free Port**") in addition to a number of laws introducing amendments to related legislative acts.

The Vladivostok Free Port regime is established for an initial period of 70 years and may be extended by federal law.

The Vladivostok Free Port enjoys a number of benefits, including simplified visa regime, tax holidays and administrative benefits. The details of all benefits available to the residents of Vladivostok Free Port are provided in Table 2 on page 5.

## Territories of Accelerated Development

In addition to the Vladivostok Free Port regime, a number of territories within the Russian Far East region benefit from special treatment incentivizing investment and business operations in the region established by Federal Law No. 473-FZ "On Territories of Accelerated Social and Economic Development in the Russian Federation" dated 29 December 2014 ("**Law on Territories of Accelerated Development**").

The territories of accelerated development benefit substantially from the same tax, customs and administrative benefits as the Vladivostok Free Port. (The details and specifics are provided in Table 2 on page 5.)

In contrast to Vladivostok Free Port, the territories of accelerated development are focused on specific areas or industries, and the benefits are allocated accordingly. As of 1 October 2017, there are 18 territories of accelerated development within the Russian Far East recognized by the regulations established under the Law on Territories of Accelerated Development as further described in Table 1 below.

**Table 1. Territories of Accelerated Development (as at 1 October 2017)**

No.	Territory of Accelerated Development	Focus of development	Location within the Russian Far East
1	Amuro-Hinganskaya	<ul style="list-style-type: none"> <li>agricultural industry</li> </ul>	Jewish Autonomous region
2	Belogorsk	<ul style="list-style-type: none"> <li>agricultural industry</li> <li>manufacturing industry</li> </ul>	Amursky region
3	Beringovsky	<ul style="list-style-type: none"> <li>extraction of minerals</li> <li>port activity</li> <li>transport and logistics hub</li> </ul>	Chukotka peninsula
4	Bolshoy Kamen	<ul style="list-style-type: none"> <li>agricultural industry</li> </ul>	Primorsky region
5	Gorniy Vozdukh	<ul style="list-style-type: none"> <li>agricultural industry</li> </ul>	Sakhalin island
6	Kangalassi	<ul style="list-style-type: none"> <li>manufacturing industry</li> </ul>	Sakhalin island
7	Kamchatka	<ul style="list-style-type: none"> <li>port activity</li> <li>air cargo shipments</li> <li>manufacturing industry</li> <li>tourism cluster</li> <li>forestry industry</li> <li>metallurgy</li> <li>industrial and household waste utilization</li> </ul>	Kamchatka peninsula
8	Komsomolsk	<ul style="list-style-type: none"> <li>manufacturing industry</li> </ul>	Khabarovsk region
9	Kurily	<ul style="list-style-type: none"> <li>agricultural industry</li> </ul>	Sakhalin island

No.	Territory of Accelerated Development	Focus of development	Location within the Russian Far East
10	Mikhailovsky	<ul style="list-style-type: none"> <li>agricultural industry</li> </ul>	Primorsky region
11	Nadezhinsky	<ul style="list-style-type: none"> <li>manufacturing industry</li> <li>transport and logistics hub</li> </ul>	Primorsky region
12	Neftekhimicheskiy	<ul style="list-style-type: none"> <li>petrochemical industry</li> </ul>	Primorsky region
13	Nikolaevsk	<ul style="list-style-type: none"> <li>agricultural industry</li> </ul>	Khabarovsk region
14	Priamursky	<ul style="list-style-type: none"> <li>manufacturing industry</li> <li>transport and logistics hub</li> </ul>	Amursky region
15	Svobodniy	<ul style="list-style-type: none"> <li>gas-processing industry</li> </ul>	Amursky region
16	Khabarovsk	<ul style="list-style-type: none"> <li>agricultural industry</li> <li>manufacturing industry</li> <li>transport and logistics hub</li> <li>food manufacturing industry</li> <li>metallurgy</li> </ul>	Khabarovsk region
17	Yuzhnaya	<ul style="list-style-type: none"> <li>agricultural industry</li> </ul>	Sakhalin island
18	Yuzhnaya Yakutiya	<ul style="list-style-type: none"> <li>extraction of minerals</li> </ul>	Republic Sakha (Yakutia)

## Benefits Available to Residents of Vladivostok Free Port and Territories of Accelerated Development

The below chart sets out a brief summary of the key benefits and incentives available to companies and individual entrepreneurs that are residents of Vladivostok Free Port and territories of accelerated development.

**Table 2. Summary of Benefits and Incentives**

Type of Benefit or Incentive	Description	Free Port Vladivostok	Territories of Accelerated Development
<b>Tax</b>	Decreased profit tax rate: <ul style="list-style-type: none"> <li>federal profit tax rate: 0% for the first 5 years; 2% for the next 5 years</li> <li>regional profit tax rate: 5% or less for the first 5 years; at least 10% for the next 5 years</li> </ul>	✓	✓
	Land tax holidays	✓ for first 5 years	✓ for first 3 years

<b>Type of Benefit or Incentive</b>	<b>Description</b>	<b>Free Port Vladivostok</b>	<b>Territories of Accelerated Development</b>
	Decreased property tax rate	✓ 0% for first 5 years; ✓ 0.5% for the next 5 years	✓ 0% for first 5 years; ✓ 1.1% or less for the next 5 years
	Decreased insurance premiums rate of 7.6% (compared to 30% for no-residents) for mandatory pension, social (for temporary incapacity to work and maternity) and medical insurance	✓	✓
	Accelerated VAT refund procedure that takes not more than 10 days	✓	✓
	Limitations on the number, scope and duration of tax inspections by Russian tax authorities	✓	✓
<b>Customs</b>	Free customs zone regime that allows duty-free import and re-exportation of goods and equipment originating from outside of Russia	✓	✓
<b>Administrative</b>	Limitations on the number, scope and duration of inspections by Russian governing authorities, including in respect of industrial safety and environmental protection	✓	✓
	Exemption from limits (quotas) on the number of foreign employees otherwise applicable and simplified procedure for obtaining work permits for foreign employees	✓	✓
	Protection of residents' rights through special powers of the Management Company (discussed below) to represent residents in court	✓	✓
	Lease of the state or municipal land plots	A simplified procedure for the lease of state land plots without a tender or auction	The right to lease state or municipal land plots on favourable terms. After the fulfilment of conditions of the implementation activities agreement

Type of Benefit or Incentive	Description	Free Port Vladivostok	Territories of Accelerated Development
			the Management Company transfers the land plot's title to the resident.
	Term for obtaining authorizations required for capital construction projects	Shortened term that is not exceeding 40 days	Regular term
	One-window approach	-	✓
	Multifunctional centre for provision of state services	-	Such functions are carried out by the Management Company
<b>Simplified Visa Regime</b>	Citizens from China, Japan, Singapore and 15 other named countries have a right to file online application for a short-term visa. The application must be filed at least 4 days prior to entering Russia. The visa is issued free of charge and is valid for 30 days from the date of issuance for a stay in Russia for up to 8 days.	✓	-

The legislation and governmental decisions with respect to the Vladivostok Free Port and the territories of accelerated development special regime contain specific provisions concerning the respective requirements for infrastructure development and the sources of financing available for such infrastructure development (if any), including monies from the extra-budgetary sources as well as regional and municipal budgets.

## Becoming a 'resident' of Vladivostok Free Port or Territory of Accelerated Development

In order to enjoy the benefits described in Table 2 above, a company (or individual entrepreneur) must first obtain the status of a 'resident' of Vladivostok Free Port or a territory of accelerated development (as applicable). In order to do this, the company (or individual entrepreneur) must submit an application and enter into an agreement with the local authorities for the implementation of its operations. After which the company (or individual entrepreneur) will be registered in the register of residents of Vladivostok Free Port or a territory of accelerated development (as applicable).

Legislation provides that an application for becoming a resident should be approved if the applicant:

- is established and registered on the territory of Vladivostok Free Port or a territory of accelerated development (as applicable);
- intends to carry out:
  - a new investment project or a new type of business activity corresponding to the criteria established by the Law on the Vladivostok Free Port (but expressly not being involved in activities that are prohibited to be undertaken by residents of the Vladivostok Free Port,

such as oil and gas production, administrative activities and related supplementary services (other than renting and leasing), and manufacture of excisable goods (other than the production of passenger cars, motorcycles, motor oils, aircraft, diesel and auto fuels)); or

- a listed type of business activity in a respective territory of accelerated development;
- anticipates capital expenditures of at least (i) 5,000,000 roubles (approximately 84,000 US dollars) for the Vladivostok Free Port within three years from its inclusion in the register of residents or (ii) 500,000 roubles (approximately 8,700 US dollars) for territories of accelerated development;
- does not have debts for taxes greater than 25% of its asset book value (pursuant to Russian accounting standards); and
- is not subject to a reorganisation, liquidation or insolvency procedure.

Following approval of the application for residency, the applicant enters into an agreement with local authorities for the implementation of its operations within the Vladivostok Free Port or a territory of accelerated development (as applicable). The agreement is concluded for a term proposed by the investor and establishes the terms of the investment program, including the investor's obligations to conduct certain activities and to make capital investments in the amounts and within the time periods set out in the agreement.

## Management of the Vladivostok Free Port and Territories of Accelerated Development

The regulation and management of the Vladivostok Free Port and territories of accelerated development is carried out by the following authorities:

- **Ministry of the Far East:** The Ministry for the Development of the Russian Far East is responsible for overall regulation and supervision of the Russian Far East development. Also it has certain specific business related functions such as establishing the procedure for maintaining the residents registers, granting long-term lease rights or easements with respect to state land plots;
- **Supervisory Board:** It is a collegial body consisting of representatives of federal and local governing bodies that is in charge of general supervision over business and social activities;
- **Management Company:** JSC Far East Development Corporation is a wholly state owned company charged with daily management of the Vladivostok Free Port and the territories of accelerated development, including with respect to conclusion of agreements with applicants required for obtaining the status of a resident and monitoring the compliance with the terms of such agreements.
- **Public Council:** The Law on Vladivostok Free Port also envisages establishment of an advisory body composed of representatives of trade unions, business associations, etc. However, as at 1 October 2017 the Public Council has not yet been formed.

The Russia Far East region is also regulated and managed by the specifically established authorities and institutions set out in Table 3 below.

**Table 3: Governmental authorities and management institutions**

Name	Description	Functions
The Ministry for the Development of the Russian Far East	The Federal Ministry of the Russian Federation	<ul style="list-style-type: none"> <li>• coordinates the implementation of state programs and federal targeted programs;</li> </ul>



Name	Description	Functions
		<ul style="list-style-type: none"> <li>• manages federal property located in the Russian Far East; and</li> <li>• oversees the execution of the powers delegated to the regional authorities.</li> </ul>
The Far East Investment and Export Agency	Autonomous non-commercial organization founded by the Ministry for the Development of the Russian Far East	<ul style="list-style-type: none"> <li>• attracts investors to the Russian Far East;</li> <li>• assists in the preparation and realisation of investment project in the Russian Far East;</li> <li>• consults, informs and organises support of investors, trade partners, and exporters; and</li> <li>• promotes export.</li> </ul>
The Far East Human Capital Development Agency	Autonomous non-commercial organization founded by the Ministry for the Development of the Russian Far East	<ul style="list-style-type: none"> <li>• oversees labour resource acquisition of the Russian Far East;</li> <li>• oversees demographic and migration development;</li> <li>• develops educational and social projects; and</li> <li>• promotes the Russian Far East as a place for life and work.</li> </ul>
JSC Far East Development Corporation	A state-owned joint-stock company	<p>is Management Company for:</p> <ul style="list-style-type: none"> <li>• the territories of accelerated development;</li> <li>• the Vladivostok Free Port.</li> </ul>
The Far East Development Fund (FEDF)	<p>The Fund established by the State Corporation "Bank for Development and Foreign Economic Affairs (Vnesheconombank or VEB)".</p> <p>As of June 2017 total assets of the Fund amounted to 32.7 billion roubles (approx. 573.6 million US dollars).</p>	<ul style="list-style-type: none"> <li>• provides preferential financing (at 5% APR in roubles) to the investment projects in the Russian Far East; and</li> <li>• provides long-term financing of prioritised investment projects in various industries (infrastructure, upstream and downstream production of minerals, support of SMEs, agriculture, etc.) in the Russian Far East.</li> </ul>

Name	Description	Functions
The Far Eastern Fund for Developing and Implementing High Technology	<p>The Fund established by FEDF, Rosnano and JSC Russian Venture Company.</p> <p>The target amount of the Fund's total assets is 10 billion roubles (approx. 175 million US dollars).</p>	<ul style="list-style-type: none"> <li>provides debt financing for Russia Far East companies that develop advanced technologies; and</li> <li>finances projects related to the transfer of technology from abroad, the expansion and modernisation of production of technological products.</li> </ul>

## Special economic zones

In addition to the Vladivostok Free Port and the territories of accelerated development, there are two special economic zones established within the Russian Far East: in Magadan region and in Vladivostok.

A special economic zone is a delimited territory where a different regime for conducting business is established in order to incentivize business and investment.

### Special economic zone in Vladivostok

In 2014 an industrial production special economic zone was established in Vladivostok with the initial term of 49 years. The priority development fields of this zone are:

- auto manufacturing;
- automotive components;
- instrument manufacturing;
- constructional materials;
- medical equipment;
- construction machinery;
- household appliances;
- IT facilities.

The residents of the special economic zone in Vladivostok benefit from the following:

- reduced profit tax rate:
  - 3% for the first 5 years since the receiving of the first profit;
  - 13% for the next 5 years;
- 10 year tax holidays for the property tax;
- 5 year tax holidays for the land tax;
- a decreased insurance premiums rates;
- a duty-free zone procedures.

### Special economic zone in the Magadan region

The special economic zone in the Magadan region was established by federal law in 1999. It is not limited to any specific areas of priority development, therefore, any operations can enjoy the established benefits, save for those that are expressly excluded by law. The following operations are

not entitled to the benefits otherwise available to residents of the Magadan region special economic zone:

- oil and gas production and services;
- manufacture of excisable goods with the exception for production of passenger cars and motorcycles;
- wholesale and retail trade;
- provision of residential maintenance and services;
- production and maintenance of weapons and military equipment.

Residents of the Magadan region special economic zone benefit from the following:

- tax:
  - (i) reduced profit tax rate;
  - (ii) reduced mineral extraction tax coefficient;
  - (iii) reduction of their tax base by 100% of their losses (compare with ordinary taxpayers who are allowed to reduce their tax base by only 50% of their losses).
- customs: duty-free import and re-exportation of goods and equipment originating from outside of Russia.

## Regional investment projects

In addition to the above described programs and incentives, the Russian Tax Code also provides for a number of tax benefits aimed at incentivizing regional investment projects, including projects in the Russian Far East; however, this regulation is not specific to the Russian Far East only.

In order to benefit from such incentives, a project must meet certain requirements, including:

- it is production-oriented;
- it is conducted in certain territories (all territories of the Russian Far East meet this requirement);
- it is not focused on:
  - (i) the extraction, production and (or) transportation of oil and gas;
  - (ii) the production of excisable goods (except motorcycles and cars); or
  - (iii) the conduct of any activity that already benefits from zero profit tax rate;
- the volume of capital expenditures envisaged by such project must not be less than:
  - (i) 50,000,000 roubles if the participant of the regional investment project ("**RIP Participant**") is to complete its investment within three years from its inclusion in the RIP Participants' register; or
  - (ii) 500,000,000 roubles if the RIP Participant is to complete its investment within five years from its inclusion in the RIP Participants' register.

The tax benefits available to RIP Participants include, among other things, the following:

- **Alternative Taxation Schemes.** RIP Participants may choose between the following two profit taxation schemes:

### Option One:

The profit tax rate is set between 0% – 10% for first five years starting from the RIP Participant's first year of profit and between 10% – 17% for the following five years.

- The regional portion of the RIP Participant's profit tax rate is set by the decision of the applicable regional authorities and the federal portion of the RIP Participant's profit tax

rate is 0% for all ten years of the privileged tax regime.

- If within the first three years of a project with less than 500,000,000 roubles of capital expenditures it does not become profitable, the term for application of reduced tax rates will start to have effect in the 4th year of the project's life.
- If within first five years a project with 500,000,000 roubles or more of capital expenditures does not gain any profit, the term for application of reduced tax rates will start to have effect in the 6th year of the project's life.

#### Option Two:

The profit tax rate is set between 10% – 17% for the entire period from the RIP Participant's first profit until the RIP Participant recovers its capital investments.

- The regional portion of the RIP Participant's profit tax rate is set by the decision of the applicable regional authorities and the federal portion of the RIP Participant's profit tax rate is 0% for the entire period of the privileged tax regime.
- **Reduced Property Tax.** The regional authorities are entitled to reduce the RIP Participant's property tax rate on a case-by-case basis.
- **Reduced Land Tax.** The municipal authorities are entitled to reduce RIP Participant's land tax rates on a case-by-case basis.
- **Reduced Mineral Extraction Tax.** The Tax Code provides for reduced mineral extraction tax coefficient (for extraction minerals other than hydrocarbons).

## Other Russian Far East Development Initiatives

### Tourism and Casino

Russian Far East also includes the Primorskoye entertainment zone which is one of the four entertainment zones where gambling is permitted in Russia (since 2006 gambling (other than bookmaking and betting) has been prohibited in Russia except for specially allocated zones). The Primorskoye entertainment zone comprises over 600 hectares (approximately 1,483 acres) of land that can be used for the development of various entertainment centres, casinos, hotels, yacht clubs and other tourist facilities. The first casino Tigre de Cristal was opened in the Primorskoye entertainment zone in October 2015.

In addition, the Russian Tax Code entitles companies who conduct tourism and recreation activities in the Far East region to apply a zero profit tax rate since 1 January 2018 till 31 December 2022.

### Shipbuilding and Ship Repair Cluster

The Russian Far East is to become home to the first of its kind in Russia shipbuilding and ship repair cluster. The cluster is going to be formed on the base of JSC Far Eastern Shipbuilding and Ship Repair Center (FESRC) enterprises. The project is centered around the construction of the shipbuilding centre at existing ship repair facility Zvezda in the town of Bolshoi Kamen, 12 miles northeast of Vladivostok.