Tax incentives in Far Eastern Russia
Investor Perspective

On 30 September 2013 a law was introduced in the Russian Federation providing profits tax and mineral resources extraction tax incentives to investors in certain regions of Far Eastern Russia and Siberia. These incentives came into effect from 1 January 2014 and are likely to make Far Eastern Russia an extremely attractive region for manufacturers.

Benefits

The law removes the federal part of the tax rate for ten years, which means that the profits tax rate is lowered from 20% to 18% for qualified projects.

Each region can adopt changes to regional laws and decrease the regional part of the rate. The majority of regions has adopted such changes (e.g. the regional portion of the profits tax for investors in Sakha (Yakutia) Republic and the Khabarovsk territory will be 0% for the first five years and 10% for the next five years). If other regions do not make any changes, the regional portion of the profits tax will be 10% for the first five years and 18% for next five years.

In addition, the **mineral resources extraction tax rates** for investors will be:

- Not payable for the first two years
- Reduced by 80% for the third and fourth years
- Reduced by 60% for the fifth and sixth years
- Reduced by 40% for the seventh and eighth years and
- Reduced by 20% for the ninth and tenth years.

Requirements

In order to qualify for the tax incentives, a company must fulfil the following requirements:

- Must be a Russian legal entity registered in one of the specified regions and with no subdivisions located in other regions.
  The following 13 regions are specified:
  – the Republics of Buryatia, Sakha (Yakutia), and Tyva;
  – Zabaikalsk, Kamchatka, Primorsk, and Khabarovsk territories;
  – Amur, Irkutsk, Magadan, and Sakhalin regions;
  – the Jewish Autonomous Region;
  – the Chukotka Autonomous District.
- Must be a producer of goods (except for Oil & Gas and excisable goods). The income of the company from sales of goods produced under an investment project must amount to 90% of the taxable income.
- Must have a minimum investment (CapEx) of RUB 50 million over three years maximum or RUB 500 million over five years maximum. Investments for the modernisation of current assets also qualify.

Each region can adopt changes to regional laws and introduce additional qualifying criteria (e.g. Tyva and Primorsk additionally require from the investor the creation of certain number of working places and specify the priority industries).

Issues for consideration

- Investors will be required to prepare certain documents proving their compliance with the requirements, including an investment declaration to be included in the register of investors and investment projects. The first stage is therefore to take compliance actions, then make qualified investments, which will result in lower rates.
- Separate tax accounting for project and non-project activities must be maintained, which may create challenges in certain cases.
- The incentives only cover the producers of goods, but the definition of "goods" is not clear and requires more detailed guidance.
- The period of application of the incentives may be insufficient for some large investment projects with long payback periods.
- No retrospective claims are possible.
- Other legal entities should not have buildings on land plots where the project is performed.

How Deloitte can help

Deloitte has wide-ranging successful experience in assisting clients with regional tax incentives at all stages. As we took an active role in the elaboration of the law, we have a good understanding of its pitfalls. Thanks to our expertise, our clients can address any relevant risks in advance and maximise the effectiveness of their claim.

Though our role in the process of claiming the incentives and adding value to the company may vary significantly depending on the specific case, we can typically help with the following:

- Elaboration of a detailed plan/strategy for applying the lower profits tax rate. Based on an analysis of the company's situation we identify actions that need to be carried out, risks that need to be addressed (if any), and help to substantiate unclear positions. As a result, the company is provided with a detailed roadmap and risk mitigation strategy.
- Compliance support. We help to prepare all necessary applications and facilitate the submission of papers to the authorities (particularly in cases where the company lacks the resources to do this itself).

As investments can only be considered qualified after filing an application, an early feasibility study can help to maximize the effects. In our experience, some specific client cases require clarification with the Ministry of Finance or negotiations with regional governments.

Contacts

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